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Politics this week

Dec 5th 2002
From The Economist print edition

Inspections continue

Reuters

The UN's weapons inspectors continued to monitor suspect sites with **Iraq's** co-operation. Iraq promised to deliver a list of weapons programmes on December 7th, a day ahead of time. Meanwhile, America pursued its preparations for war, and, with Britain, intensified its bombing of Iraq's air-defences in the “no-fly zones”. Turkey said it would offer facilities to American forces but only if the UN passed a second resolution endorsing military action.

See article: No bombs here, honest

A 44-country poll by the Pew Research Centre found a rise in **anti-Americanism** over the past two years, mainly in the Muslim nations of the Middle East and Central Asia.

Egypt's highest appeal court quashed the seven-year sentence on Saadeddin Ibrahim for defaming his country and accepting foreign money. But Mr Ibrahim, a social scientist, now faces a new trial, his third, next month.

Israel's prime minister, Ariel Sharon, said that he accepted President George Bush's plan for a **Palestinian state** with temporary borders. But Palestinians said Mr Sharon's proposal for only 42% of the West Bank was unacceptable. And right-wing members of his coalition said such a state would pose an “existential threat” to Israel.

See article: Israel's wartime politics

The World Food Programme gave warning that 18m people were at risk of **starving** in Ethiopia, Eritrea and Sudan; 16.4m were at risk in southern Africa and 2.7m in Africa's Great Lakes region.

The government of **Burundi** and the main rebel group signed a ceasefire. More than 300,000 people have been killed in nine years of war.

Kenya has so far arrested 13 people in connection with last week's bombing of a Mombasa hotel. Britain closed its mission in Nairobi after “a specific threat”.

Catholic tastes

Scandal engulfing Boston's **Catholic church** deepened after archdiocesan files newly released by court order showed that senior figures were more aware of claims of sex and drug abuse by priests than they had admitted. The files were obtained by one of some 450 defendants suing the archdiocese, which is said to be considering Chapter 11 bankruptcy protection.

See article: The Roman Catholic church in Boston

John Kerry, a Massachusetts senator, launched a preliminary campaign for the Democratic presidential nomination in 2004.

See article: Another Democratic contender

The **Supreme Court** said it would hear cases brought by three white students who claim that, because of an “affirmative action” programme, their places at the University of Michigan were given to black and Latino students who had done no better.

See article: End affirmative action

Adel al-Jubeir, Crown Prince Abdullah's foreign-policy adviser, told a press conference in Washington that **Saudi Arabia** had been smeared by criticism that it had not done enough to support the war on terrorism since September 11th. Meanwhile, Prince Nayef bin Abdul-Aziz, the Saudi interior minister, told a Kuwaiti newspaper that Zionists were behind the terrorist attacks.

New members welcome?

The **European Union** and its would-be new members pushed on with final negotiations before the Copenhagen summit due to start on December 12th. But would Turkey be given a date for starting its negotiations? That was still uncertain, despite trips to many EU capitals by Recep Tayyip Erdogan, leader of Turkey's now ruling AK party.

See article: The European Union expands

A blow to the EU's planned Airbus-built **A400M** heavy-lift military aircraft: Germany is likely to order only 60, instead of the 73 at one time talked of.

Fresh swathes of **oil** spilled by the now sunken tanker *Prestige* spread further along the north-western coasts of Spain. While politicians there exchanged insults over the sluggish and ill-equipped official response, the EU prepared plans for an early ban on the carriage of heavy oil by single-hulled tankers.

See article: The Prestige oil spill

France's government agreed to close the Sangatte “refugee” centre near Calais, a source of much British anger, at the end of December, four months earlier than planned. But Britain agreed to allow (provisional) entry to a large number of the inmates.

Reuters

The **Danish** government formally rejected Russia's call for the extradition of Akhmad Zakaev, a Chechen leader, saying that evidence that he was a terrorist was “insufficient”.

Call to arms

In an unusually tough speech even for a hardliner, L.K. Advani, India's deputy prime minister, dared Pakistan to fight “face to face” instead of supporting terrorist groups in Indian-run **Kashmir**. “Let there be a fourth war,” he said. India has fought three wars with Pakistan, two of them over Kashmir.

Five people were reported dead in Dili, the capital of **East Timor**, when police fired on a crowd protesting against the arrest of a student. The prime minister's house was burnt down.

The Australian prime minister, John Howard, said he was prepared to strike pre-emptively at militants in other countries if they threatened **Australia**. Malaysia, Indonesia, Thailand and the Philippines, none of them named by Mr Howard, responded angrily. Police in Indonesia claimed to have arrested the mastermind of the Bali bombings in which many Australians died.

See article: Security after Bali

An American B-52 bombed an area of western **Afghanistan** in support of American soldiers caught in a battle between rival Afghan warlords.

See article: Securing peace

At a meeting in Beijing, the Chinese and Russian leaders, Jiang Zemin and Vladimir Putin, called on **North Korea** to stop its nuclear-weapons programme and for the United States and North Korea to normalise diplomatic ties.

See article: Old allies turn on North Korea

In a bid to ease Australia's **drought**, 200 farmers' wives in Victoria planned a naked rain-dance, similar to one said to have brought much-needed rain to Nepal.

Strike force

In **Venezuela**, opponents of President Hugo Chavez called a general strike, extended for several days, in an effort to force the president to hold an early referendum on his rule.

See article: Venezuela's escalating strike

The United Self-Defence Forces of **Colombia**, the country's main paramilitary group, announced a ceasefire from December 1st, apparently in the hope that the government would drop legal proceedings against it. America's secretary of state, Colin Powell, visited Bogota to support President Alvaro Uribe and implied that he would get more aid.

See article: Colombia's paramilitaries announce a ceasefire

A report on **Canada's health system**, said that C$15 billion ($10 billion) was needed to modernise and streamline it, but that more private provision was unnecessary.

See article: Health-care reform in Canada

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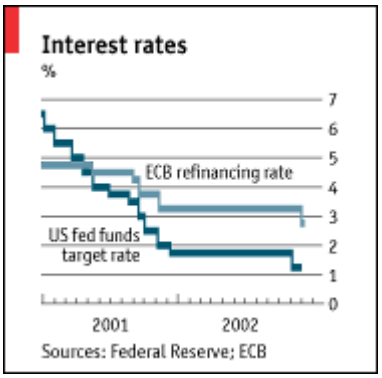
Business this week

Dec 5th 2002
From The Economist print edition

Half measure



The European Central Bank fulfilled expectations and cut **interest rates** by half a percentage point to 2.75%. A probable further easing of inflationary pressures and the likelihood of sluggish growth encouraged the bank to heed the calls of Europe's businesses for a cut.

See article: European interest rates

America's productivity grew by an impressive 5.1% at an annual rate in the third quarter, outstripping forecasts. Productivity often bounces in the first year of a recovery as workforces have been trimmed; but the pace of growth is a sign that the economy is now reviving.

See article: The economy keeps growing

United falls

The federal Air Transportation Stabilisation Board rejected **United Airlines**' request for a $1.8 billion loan guarantee. United had secured wage concessions from many employees and had been planning to re-ballot mechanics, who had voted against wage cuts. The airline now has no alternative to Chapter 11 bankruptcy.

See article: United on the brink

American Airlines said it would shed 1,100 flight attendants to save cash. Recently, it has announced big cuts to its domestic services.

Credit crunch

BNP Paribas turned up the heat on Crédit Agricole, a rival for control of Crédit Lyonnais. It added to a 10.9% stake bought from the French government by acquiring another 5.3% in the market. Crédit Agricole, meanwhile, parted company with its chairman, Marc Bué. His replacement, René Carron, is considered more suitable for the scrap over Crédit Lyonnais.

See article: Crédit Lyonnais

Barclays gave a surprise warning that profits for the year were unlikely to exceed last year's pre-tax return of £3.4 billion ($5.1 billion). Britain's fourth-largest bank is suffering from rising bad-debt provisions and “tough” business conditions; its shares tumbled. **Lloyds TSB** also gave warning of higher provisons for bad debts and exposure to Argentina and Brazil.

The travails of the life-insurance industry led Australia's **AMP** to add a further 1,900 job losses to the 1,500 announced in June. The cuts will come at Pearl, a British life-insurance company.

Victory for Vivendi

Vivendi Universal won the battle for control of Cegetel. It exercised its pre-emptive right to buy a 26% stake in France's second-largest telecoms company from BT for *euro*4 billion ($4 billion), thwarting (for now) Vodafone's designs on the company. Vivendi also hinted that it may eventually demerge Universal, its American entertainment business.

See article: Does Vivendi have a strategy?

Deutsche Telekom's new boss, Kai-Uwe Ricke, made his first dent in the German telecoms giant's prodigious debts of some *euro*64 billion ($64 billion). DT chipped $610m off the debt mountain through the sale of around 8% of T-Online, its Internet arm.

AOL Time Warner gave a gloomy forecast for America Online, its Internet division: flat revenues and falling profits in 2003, as advertising and e-commerce revenues suffer. The company put its faith in a revival through winning broadband subscribers with the lure of premium content.

Long gone silver

Disney restated its profits for the year to the end of September after its latest animated release—the inaptly named “Treasure Planet”—sank at the box office.

Massachusetts plans to appeal against the antitrust settlement with **Microsoft**. It and eight other states rejected the deal for its leniency, but were turned down by the courts. Seven states then accepted that verdict; West Virginia will also appeal.

America's big three car makers had a torrid November in home markets: **Ford's** sales fell by 17%, **GM'S** by 18% and **DaimlerChrysler's** by 12%. In contrast, **Porsche** is in line for a bumper year, after the German luxury-car maker sold its entire annual 25,000 production run of its new sport-utility vehicle before they were released to dealers.

AmeriKing, one of **Burger King's** biggest American franchisees, filed for Chapter 11 bankruptcy. Despite the news, Diageo is expected to go ahead later this month with the sale of its fast-food hamburger business to a group led by Texas Pacific, an American private-equity firm.

See article: An industry suffering from indigestion

Russia's government announced the sale of part of its 13.5% stake in **Lukoil**. It had planned to sell 5.9% of the oil company earlier in the year, but put it off because of its depressed share price. This time, state coffers could be swelled by up to $800m.

Creditors of **Enron** will be disappointed to note that the “crooked E” adorning the failed energy group's Houston headquarters sold for only $10,500. A similar sign sold for $45,000 in September, but prices have since collapsed.

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Europe and Turkey

Turkey belongs in Europe

Dec 5th 2002
From The Economist print edition

The European Union should be willing to bring Turkey into its ever-growing club

Get article background

A NEW map of the old continent is unrolling at a dizzying speed. It now seems very likely that by the end of next week a European Union of 15 countries containing some 370m people will have asked another ten countries with 90m more people to join the show. This invitation comes a bare month after NATO asked another seven countries, most of them in that same batch of would-be newcomers to the EU, to join the world's greatest military alliance. A mere decade-and-a-half ago, when the world's pair of then superpowers—the United States and the Soviet Union—were glowering at each other across a nervous European continent divided by barbed wire and antagonistic ideologies, the notion of so dramatic a turnabout would have been absurd.

A Union based on values

Yet even these extraordinary events pale beside what may well be the trickiest conundrum for Europe's leaders when they meet next week in Copenhagen. That is the question of whether Turkey, a Muslim country of nearly 70m souls, which is already part of NATO, should be invited, with real intent provided that the applicant meets rigorous conditions, to join Europe's top civilian club too. It is a massive question, because it raises the issue of where the geographical boundaries of the EU should end. Might Russia itself, one day, be included? Could Morocco ever make the grade? Indeed, if Turkey joined, why not, one day, its neighbour, Iraq?

If the European idea is to inspire, it ought to be about values, not maps or tribes

It is hard to answer that question without deciding what the ultimate purpose of the EU is. But here there is no consensus: the habit of the EU has been to invent itself as it goes along. Its shape and purpose are evolving. It is plainly becoming a hybrid: much more than just a free-trade area but much less than a superstate. For many of its members, not just for those awkward Britons but also for prickly newcomers such as the 40m Poles, a headlong drive towards political and even military integration will be resisted. *The Economist* would prefer this looser sort of Europe, perhaps comprising overlapping inner clubs of those who wish to integrate more tightly. As for Russia, or Morocco, why should geography, or religion, dictate who might join? If the European idea is to inspire, it ought to be about values, not maps or tribes. Countries that can subscribe to the core values of democracy and freedom should be eligible as candidates, be they Slavs or Muslims, and no matter how far they are in miles from Paris or Berlin.

At some point, any club bumps into the danger of growing so big that the benefits of belonging to it are diluted. If the EU continues to insist on every new member adopting its common currency, the laws of economics mean that the limit will be reached sooner rather than later. But no such question of optimal size is raised by the question of Turkey. The Turks want Europe, as a mark of sincerity, to name at least a date when, provided that progress towards market stability and a better upholding of human rights continues, they can start formally negotiating for entry into the EU—even though they know they are unlikely to be ready for actual membership for another 10-15 years. The Europeans should agree.

That does not mean that there are no reasons to be wary. Once negotiations have begun, it will be

harder later, at any time, to reject Turkey without provoking the same anti-western and even anti-Christian fury that an invitation is meant to dispel. And it is true that, as things in Turkey stand, progress will have to speed up still more if it is to qualify even for starting negotiations. An admirably radical reform package enacted in August and further proposals put forward this week still need implementing. The treatment of dissidents, ethnic minorities and ordinary prisoners must yet improve: torture is less frequent but still common. The loosening of restrictions against the Kurdish language in broadcasting and education is still tentative. The generals still have too great a say in politics. The market economy is fragile. A strong new government with a big majority in parliament and Islamic roots in the country has made a good start. But it is early days. An unconditional promise to start negotiations would be silly.

Moreover, those in Western Europe who question where the EU would end and what sort of Union would evolve if 70m Turks became part of it have a point. Membership for a country whose land mass is overwhelmingly in Asia would indeed be anomalous. And at a time when Europeans are gathered at a convention in Brussels to produce ways of streamlining decision-making and to make the running of the EU more understandable to its citizens, it may seem odd to digest yet another country that may well, if demographic trends continue, become the Union's largest in a generation or so.

But the reasons for being bold and generous towards Turkey are stronger still. It straddles east and west. Its finest historic landmarks are indubitably in Europe—on the western side of the Bosporus. As a longstanding NATO member, it has been a crucial part of Europe's defences. It has been a beacon of good sense in a combustible bit of the world. And as part of any deal, Turkey's new government would be expected to squeeze its hitherto recalcitrant cousins in Cyprus into accepting the latest sensible idea presented by the United Nations for a loosely confederal system.

The tie that could bind Islam and the West

Perhaps most important, an EU that is open to Turkey should send a message to the troubled Muslim world of today: the West does not consider Islam and democracy incompatible as long as Islam doesn't. Within the EU's current borders live a good 15m or so Muslims, whose rights are well protected in law. Albania and Bosnia, both states with partly Muslim heritages, should be equally valid candidates, eventually, for EU membership. Later, the net might stretch wider still.

Since the Ottoman empire's fall, Turkey has been at best a sporadic and flawed democracy with weak traditions of civic virtue. But of late it has been improving remarkably. Offering a provisional date for the start of negotiations is an historic chance for Europe but also for the Muslim world to show that their two great civilisations are not fated always to clash.

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North Korea

The pleasure of dealing with it

Dec 5th 2002
From The Economist print edition

Decisiveness would be dangerous, but collective toughness is looking a little easier

AP

WHILE the world waits for Saddam Hussein to declare whether he has any weapons of mass destruction, matters are simpler with regard to the other totalitarian dictator who starred on George Bush's "axis of evil", Kim Jong Il. North Korea has recently admitted that it has been working on a uranium-enrichment programme in pursuit of creating nuclear weapons, in flagrant violation of four international treaties and agreements it has signed, the latest in 1994. Moreover, this week North Korea's two big neighbours and long-time patrons, Russia and China, declared their solidarity with America by calling on President Kim to renounce such weapons and ensure a "nuclear-free" Korean peninsula. All without the tiresome need for votes in the Security Council of the United Nations, or for having to sit through lectures on unilateralism or adventurism by European politicians. Disarming President Kim, by force or by diplomacy, must be only a matter of time.

The artillery trap

If only it were so. On the face of it, the case for threatening the use of military force against North Korea is even stronger than for Iraq: evidence of a weapons programme, evidence of broken treaties, evidence of hostile acts against South Korea, evidence that the regime is brutal against its own people. The difficulty, though, is that next to the "demilitarised zone" set up at the end of the Korean war in 1953 is a highly militarised zone that is well within artillery range of South Korea's capital, Seoul, which is home to more than 10m people.

In the early 1990s, when the North's previous nuclear programme was uncovered, Bill Clinton's administration worked out plans for a pre-emptive strike on the nuclear facilities, but scrapped them—not because of the worries about international law that preoccupy critics of the Bush administration's ideas on pre-emption, but simply because it was too dangerous. The North could kill hundreds of thousands of civilians in Seoul if it chose to retaliate, which it might well do, even though that would risk the regime's extinction. And there was uncertainty about how China would react if the country it rescued during the original Korean war found itself in a new one.

The circle has been closing around Kim Jong Il

That last point is what makes China's new vehemence—expressed at a Russo-Chinese summit in Beijing on December 2nd (see article)—so welcome. It will reinforce existing North Korean doubts that China would now come to its military aid if it were attacked. But it is welcome also because, given the continuing dangers of a war with the North, the best approach is a collective one, uniting all the neighbours—Russia, China, South Korea and Japan. In the past, the North has often been able to play one off against the other, or several off against America. It has succeeded in trading threats for money, a technique which, in 1994, gained it the Korean Energy Development Organisation (KEDO), a consortium formed to provide it with heavy fuel oil and new, light-water nuclear reactors in return for giving up its own nuclear programme. Such bargaining remains the likeliest motivation for the North's new clandestine nuclear project.

But what can be done about it? More together, certainly, than would have been possible apart. The circle has been closing around Kim Jong Il. During November, South Korea and Japan agreed within KEDO to an American proposal to suspend shipments of fuel oil; in mid-December, America is likely to ask them to

agree to suspend the light-water reactor project, too. They should do so; it hardly makes sense to provide a nuclear bonus to a country plainly dedicated to nuclear mischief. South Korea's presidential election, on December 19th, is likely to bring in a government keen on a harder line against the North than was the outgoing president, Kim Dae-jung, with his “sunshine policy”. Now, with this week's harder line from Russia and China, America should be able to sustain a hard line against the North rather than buying it off again—and thus rewarding its brinkmanship.

Even that, though, will not be easy. As our report from the Chinese-North Korean border shows (see article), China has a lot to fear from an economic collapse in North Korea and so is likely to resist any further tightening of economic sanctions against it. If so, that will be short-sighted: a flood of refugees would be a short-term nightmare, but sustaining North Korea's dodgy regime for ever just puts off the problem rather than solving it. Still, if China sticks to such opposition it must then be pressed to play a bigger private role in persuading Kim Jong Il to give up his weapons plan, and to accept what is likely to be America's alternative scheme: a deal to resume the KEDO oil shipments and the light-water project in return for first relinquishing the clandestine nuclear effort and undergoing a “highly intrusive” programme of nuclear inspections to police the deal. “Intrusiveness” would be vital if such a deal is to get political support in the United States, but also if it is to have any chance of working.

Next stop, Pakistan

It might never work, and war or economic collapse might prove the eventual solution. There is also, however, a wider lesson from the North Korean conundrum. It is that if you permit, or even encourage, the proliferation of the deadliest weapons or the long-range missiles with which they can be delivered, such acts are liable to boomerang against you.

That is what has happened to China. For North Korea's uranium-enrichment capability has almost certainly been obtained from Pakistan in exchange for missile technology—and Pakistan obtained its nuclear know-how from...China. Pakistan is also now an awkward American ally in the battle against al-Qaeda's brand of terrorism. Its deal with North Korea may well pre-date that new alliance, making sanctions against it for supplying the North rather pointless. China and America can, though, present a united front in persuading Pakistan never to deal again with President Kim. More important still, they can put the task of reviving and revamping the world's anti-proliferation regimes firmly on the joint agenda of all the nuclear powers. Awareness of that common interest is the silver lining to terrorism's cloud.

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Britain's top 100 jobs

How Britain's elite has changed

Dec 5th 2002
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The public schools and Oxbridge no longer dominate the top jobs

THE notion of the establishment is a powerful one in Britain. The idea that a club made up of men educated at public school (British code for smart private secondary schools) and Oxford or Cambridge runs government and business has informed much of what has been written about British politics and society for the past half-century. It has fed, and fed off, some of the most depressing ways that Britain thinks about itself. The establishment is exclusive, impenetrable and permanent. It breeds and educates its own successors. It denies those excluded from it the opportunity of rising as far as their talents would naturally take them, and it deprives the country of the chance of choosing its leaders from the largest possible pool of talent. The establishment is mediocre, uncompetitive, technophobic, snobby, and responsible for much of what went wrong in Britain in the 20th century.

Of course, this is a massive exaggeration. Clever people have always been able to make it in Britain, just as they could in any other rich society. British society is not, compared with other countries, particularly rigid. Britain's ruling class has always been rather good at absorbing outsiders. That's one of the reasons why it managed to avoid a revolution of the sort that decapitated society in so many European countries.

Yet Britain's educational system, more socially-segregated than that of any other rich country, has tended to foster a tight network at the top. Its small number of exclusive public schools and two elite universities have, to an extraordinary extent, dominated the top jobs in politics, the judiciary, the civil service, business, the church, the arts and the military.

In 1992, we looked at the educational background of the holders of 100 top jobs, and compared them with their predecessors of 20 years earlier (see article from 1992). The results were startling. Between 1972 and 1992, there was virtually no change in the proportion of top-job-holders who had been educated at public school and at Oxford or Cambridge. Ten years on, we have repeated the exercise, and the result is equally interesting, in a different way. There has now been a big drop (see article)—probably the first since the upper classes took up going to school and university—in the proportion of top-job-holders who were educated at the old elite institutions. The public schools and Oxbridge are losing their hold on power.

Several factors have contributed to this change. The biggest is probably the growth of competition that has resulted from deregulation and globalisation. Life, particularly in business, is not as cosy as it once was. Companies are larger and more multinational than they used to be, and therefore likelier to look outside the small talent-pool of familiar City types on which British business used to rely. People travel more than they used to. So today's top people's list includes more who are or used to be foreigners—such as Percy Barnevik, chairman of AstraZeneca, a Swede, and Robert Thomson, editor of the *Times*, and Patricia Hewitt, trade and industry secretary, who both come from Australia.

The transition from a Tory to a Labour government explains some of the shift, but not a great deal, because the parties are not as socially distinct as they once were. After all, neither John Major, Tory prime minister in 1992, nor Iain Duncan Smith, the current Tory party leader, went to either public school or to Oxbridge. Tony Blair is the only current party leader who went to both—or either, come to that.

A Labour government means more Scots. So does the growing power of the Scottish financial services companies. More Scots mean less Oxbridge, though not necessarily less posh, since Scotland has its own elite universities—and, of course, its own top-people's network. But more Scots do mean fewer of the English establishment types who used to run government and the City.

Government has also done its bit. Many of the successful people in this survey are the products of the grammar schools which spread around the country after the 1944 Education Act, designed to give a good education to clever children whose parents could not afford public schools. The expansion of higher education that started in the mid-1960s has also undoubtedly played a part. The top people in our survey mostly went to university in the 1960s and 1970s, when the university system was expanding fast, and the proportion of graduates who had been to Oxbridge offering themselves to employers was thus shrinking commensurately.

The wrong direction

But while those two major pieces of educational policy encouraged social mobility, a third—the fusion of grammar and secondary modern schools into a “comprehensive” secondary education system—has recently pushed in the opposite direction. This policy—under which those who had climbed the ladder are often said to have pulled it up after them—banned schools from selecting for ability and thus got rid of the fast track for the less-well-off that grammar schools had provided. Many of the best state-funded schools chose to go private as a result, so the gap between rich and poor people's education widened. Of the 100 schools that get the top A level grades now, only two are comprehensives: they rank 96th and 99th.

The abolition of grammar schools is probably one reason why recent figures suggest that social mobility in Britain has slowed: compared with children who grew up in the 1960s and 1970s, those who grew up in the 1980s had less chance of being more successful than their parents. The government, keen to encourage social mobility, is seeking to reverse this trend. It is, for instance, paying universities a premium for each student they take from poor areas and twisting their arms to get them to accept more state-school pupils.

This is unjust (because it discriminates against children because of choices made for them by their parents), damaging (because it will depress the quality of university intake) and probably ineffective. The answer is not to tweak the system when people are 18, but to provide them with better education earlier on. The government needs to re-create something like the grammar schools, to let down for the next generation the ladder up which this generation of top people climbed.

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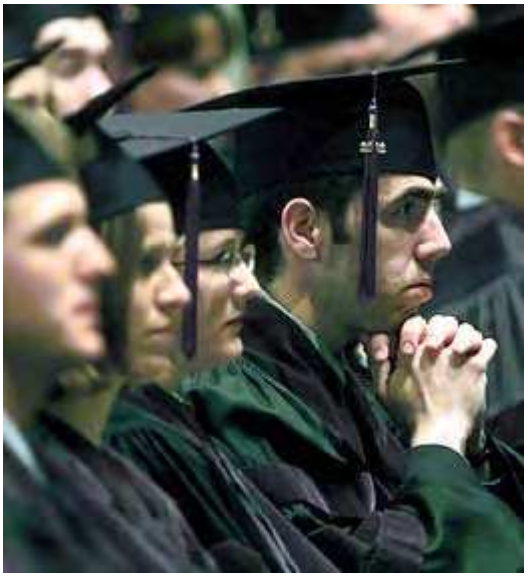
Affirmative action in America

Orwell and beyond

Dec 5th 2002
From The Economist print edition

The Supreme Court should kill a programme whose time has passed

AP



BEHIND many a modern injustice lies a good idea gone bad. “Affirmative action”, the 1960s scheme whereby blacks were given special consideration for university places (and other things), was a wise attempt to redress a grievous discrimination. For a time it worked well; it helped, for instance, to create America's growing black middle class. But it has since been extended to various other minorities, such as Latinos, Pacific Islanders and, absurdly, women. Now the idea of racially based preferences has become an Orwellian monster—outdated and ineffective at best, profoundly illiberal at worst.

This week the Supreme Court agreed to consider a case brought by three white students with good grades whose places at the University of Michigan were, they claim, given to black and Latino students who had done no better. The university's defence rests on the idea that there is a “compelling state interest” in maintaining diversity.

“Diversity” represents something of a last redoubt for defenders of affirmative action. Most people now accept that the historical argument for racial preference no longer adds up to much: slavery and Jim Crow, ghastly though they were, took place too long ago to justify, say, rejecting a poor white kid in order to let in a rich black one. Many black students worry that affirmative action devalues their achievements. Similarly, the idea that specific races deserve special protection has also been made a fool of by the melting pot. Should a black Nigerian immigrant qualify, or a “white” who has a Latino mother and an Asian grandfather? Arguably two out of three Americans now qualify as minorities of one sort or another.

E pluribus unum (sed non in Michigan)

In its last judgment, in 1978, the court struck down the idea of specific racial quotas, but it kept alive the idea that diversity in general could be a justifiable educational goal. This was intellectually sloppy. Diversity—a little like “community” or indeed “affirmative action” itself—is one of those warm and fuzzy things that are hard to oppose, but even harder to define. American universities have decided to apply it in terms of race. But why not other things—political beliefs, say—and why not apply it to teachers as well as to students? Polls have shown that only one in ten academics on some campuses vote Republican: maybe they need to be made more “diverse”.

At the bottom, affirmative action comes down to a poor piece of social policy and a profoundly illiberal principle. Social policy should be based on identifying the unfortunate by income, not colour, and helping them by direct support—making poor schools better—not by dropping standards in universities. The illiberal idea is the notion that your identity—let alone your capacity to contribute to university life—is decided by your race. That is a malignity Americans have fought wars to kill. The Supreme Court should not tolerate it.

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Palestine and al-Qaeda

From national conflict to holy war

Dec 5th 2002
From The Economist print edition

It is the Palestinians who may lose most from Osama bin Laden's adoption of their cause

AP

Get article background

HAD Osama bin Laden not proved his efficiency as a mass murderer, the world could afford to ignore the mumbo-jumbo al-Qaeda and its fellow-travellers pump out in order to justify their various atrocities. But things being as they are, the miscellany of dismal *fatwas* and communiqués that precede and follow al-Qaeda's attacks provide useful clues, both about future targets and about how the terrorists intend to mobilise wider Muslim opinion behind their cause.

One recent trend is that al-Qaeda is pushing Palestine up its list of priorities. In Mr bin Laden's 1998 declaration of holy war against “Jews and crusaders”, America's “occupation” of Saudi Arabia topped his list of grievances, the “devastation” of Iraq came second and Palestine third. However, in what looks as if it might be a genuine letter from al-Qaeda, circulated just before last week's attack, probably by al-Qaeda or an offshoot, on Israeli tourists in Kenya, the creation of Israel is described as Islam's foremost grievance against the United States.

It would be a mistake to attach too much significance to the impact of this change on the wider war against terrorism. Just at the moment, while the *intifada* growls on and Israel stamps hard on the occupied territories, it is the Palestinian cause that resonates most reliably throughout Islam, and which earns America most enemies. But al-Qaeda is nothing if not opportunistic in its propaganda. Mr bin Laden's declared grievances range widely, from Islam's loss of Muslim Spain in the 1490s to the Balkan wars of the 1990s; and to present-day conflicts in Chechnya, Kashmir, Gujarat—even East Timor, which by al-Qaeda's lights should never have been helped to independence from Muslim Indonesia. Should there be an American-led war against Saddam Hussein, Iraq will no doubt be promoted in its turn to grievance number one.

For Israelis and Palestinians, on the other hand, the attentions of al-Qaeda could have consequences that are both lasting and grievous. This is because, contrary to much conventional wisdom conceived from afar, the past half-century of conflict between Jew and Arab in Palestine has for the most part been a clash of nationalisms, not religions. The religious dimension has always existed, but the main political forces on each side have been secular in character. That has hardly made the conflict an easy one to resolve. But it could become entirely insoluble if it is Islamised. And this is precisely what al-Qaeda wants. Mr bin Laden's declared objective, directly opposite to Yasser Arafat's (at least since 1988), is to destroy Israel, not to see Palestine shared between two states.

If Mr bin Laden wins such a following among the Palestinians that he succeeds in recasting the conflict this way, the prospect of the Palestinians getting their state any time soon will recede still further. Mr Arafat himself, who was quick to denounce al-Qaeda after September 11th, plainly sees this. If the Palestinians resumed their old demand for Israel's destruction, no American administration could (or should) take their side. All the same, this has not stopped him from making far more use in this “al-Aqsa” *intifada* than in the previous one of Islamic themes, ranging from the centrality given to the mosque in Jerusalem after which the uprising is named, to Mr Arafat's constant harping on the merits of *jihad* and martyrdom. He is no doubt motivated in part by a desire to outflank the Islamists of Hamas, who have long shared Mr bin Laden's belief that Islam has a divine obligation to destroy Israel altogether, and who are gaining in influence. He should beware: religious fervour, once uncorked, is hard to put back in a bottle.

America should be wary, too. Since June, the policy of the Bush administration, urged on it by Ariel Sharon, has been to isolate Mr Arafat in the hope that he will eventually be pushed aside by a new leadership of Palestinian pragmatists better able than he was to deliver a deal acceptable to Israel. So far, the policy has failed. Mr Arafat has been weakened, but holds stubbornly on. Meanwhile it is the fundamentalists, not the pragmatists, who seem to be gaining most from his discomfiture. Only the apostles of violence will benefit from that.

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Managing in hard times

When growth is not an option

Dec 5th 2002
From The Economist print edition

Company bosses may have to get used to a different world

AS COMPANIES draw up their budgets for the year ahead, many are asking if the end of the downturn is in sight, or whether they face deeper structural changes. The recovery that now seems to be under way will probably remain relatively slow. Companies may therefore delay taking on new staff, and many industries, including airlines, telecoms and power generation, will not start buying new capital equipment for some time yet.

Even when they do, the double-digit profit growth of the late 1990s seems unlikely to return. Does this reflect deeper structural change? Some think so. Adrian Slywotzky of Mercer Management Consulting argues that much of the growth of the 1990s was bought through mergers, international expansion and price increases. Beyond the glittering numbers, companies have begun to run up against the “limits of growth”: consumers just do not want another fridge, hamburger or bank account. Markets are saturated and investment is flat. Mr Slywotzky thinks that underlying growth in some companies, such as Gillette and ExxonMobil, was negative in 1995-2000.

The uses of adversity

This limits-to-growth thesis is (mercifully) likely to prove as misleading as was Francis Fukuyama's prediction of the end of history. Most people want the quality of life that they see the rich enjoy, and that guarantees plenty of demand. But winning market share gets no easier. Demand will grow fitfully at best, as imbalances in rich-world economies are unwound. Technological change has radically altered some markets—such as advertising, where more targeted ways to reach an audience are forcing agencies to alter their approach (see article). And a fresh problem looms: managers must learn to cope with the possibility of falling prices. For most, this is an entirely new experience, previously confined to a few industries undergoing rapid change, such as telecoms and computers. Now, prices of cars, food, clothes and many services are all declining in many large markets.

How should managers respond when, in a phrase coined by Ron Nicol of BCG, another consultancy, “growth is not an option”? Part of the answer is to grasp that hard times create opportunities of their own. It becomes easier to shut down marginal capacity and cancel expensive projects with uncertain returns. When IT managers have spent lavishly, there is now a chance to insist on results. And a downturn may be a moment for the strong to buy weaker rivals.

It is also a chance to re-examine potential savings. Many companies have refined manufacturing techniques in the past decade, to the point where few further economies are to be made. But there are still savings available in more obscure parts of the business, such as the 10% or more that could sometimes be taken out of logistics (see article). Refining the delivery of parts along the chain from suppliers to the final consumer also offers a way for companies to keep inventory to a minimum—more essential than ever when prices are falling.

Above all, if companies are willing to spend a bit rather than just look for more cuts, hard times offer an opportunity to introduce structural changes essential for survival. For an example, look at Boeing. In the wake of September 11th, the aircraft maker switched to a moving assembly-line and lean-production techniques borrowed from the car industry; but it also pumped money into new investments, such as

putting high-speed satellite links into passenger aircraft and building up a new air-traffic-management business.

Learning to cope with falling prices may be the hardest challenge of all. Yet the Victorians managed it. In the great years of late 19th-century innovation and prosperity, they lived with falling prices by relying on competition, based on quality and good service. They devised brands—and used them as an assurance of quality, not just of a premium price; and they thought of ways to make customers feel truly special. Their great-grand-children must learn to do likewise.

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Letters

Dec 5th 2002
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

Breaking the borders

SIR – Clearly borders are becoming beyond control (Survey of migration, November 2nd). Many less-developed countries have social practices, political governance and economic prospects that fall far short of what developed countries can offer, leaving no policy option that can cut the outflow of skilled nationals. Developed countries have the reverse problem; they cannot control the inflow of mostly unskilled illegal immigrants and asylum-seekers. Civil-liberties activists, human-rights groups and ethnic voters (who have increased to sizeable numbers with past immigrations) will not allow draconian measures against immigrants.

Thus, we need a seismic shift of immigration policy away from attempts at curbing migration to coping with it. We also need a World Migration Organisation that could put together an impartial but complete documentation of the policies of different countries toward migrants (legal and illegal, skilled and unskilled) and other asylum-seekers. The contrast alone would propel others towards the good practices of progressive countries.

Jagdish Bhagwati
Columbia University
New York

SIR – Emigration to wealthier countries has had severe detrimental effects in developing countries. These countries invest heavily in developing human capital. We act hypocritically if we promote wealth as a means of reducing burdens to developing countries while stealing away their capacity to manage, deliver, and promote solutions.

Kevin Chan
Boston

SIR – Emigration benefits a poor country only to the extent that migrants keep ties with their old home. The policy implication is to divorce permission to work in a country from a right of permanent residence. Switzerland has long operated such a system.

This has three advantages. It encourages migrants to retain closer ties with their country of origin and take a more active interest in its affairs. It also deters free riders attracted by generous welfare systems. Finally, it would assuage the fears of those who worry that large-scale migration might lead to big (and unpalatable) cultural change.

George Stadler
Hexham, Northumberland

SIR – I am appalled at the type of proposals you put forward for controlling immigration. Limiting admission to those countries with “the same income per head” excludes a majority of the world's population. Giving preference to “those who seem to integrate most readily” smacks of an imperialist attitude. To demand that migrants are “wary of demanding special treatment in matters of dress or religious observance” is outrageous and highly intolerant. What you are advocating sets the rules for an exclusive “westerners only” club.

Dominic Bascombe
London

SIR – Migration is the shortest journey to poverty reduction. Why do rich nations say they are helping poor nations to reduce poverty when they do not allow the poor to migrate? Most of my fellow citizens who go to rich nations come back home wealthier than most of us and portray a sense of the good standard of living overseas. The world aims to reduce poverty by half by 2015. Migration, if allowed, would do the job by 2007.

Nyajro Teko
Yaoundé, Cameroon

Germany's war

SIR – I question your assertion that “The Fire”, Jörg Friedrich's newest work, breaks a long-held taboo against Germans speaking about themselves as victims of the second world war (“Another taboo broken”, November 23rd). West German social history is full of narratives about German suffering at the hands of the Nazis and the allied forces.

Until the late 1970s, German suffering was regularly equated with the suffering of the Jews in the Holocaust in public rituals and monuments. In the 1950s, former top Nazi officials were celebrated in popular film as resistance figures, such as in the hugely successful film “Canaris” (1955). In a review from the 1950s of the German-Jewish film “Long is the Way” (1948), which shows Jewish resistance and the extermination camps, a direct parallel is drawn between the suffering of Germans in air-raids and Jews in the camps. Even Günter Grass's lament that the bombing of a refugee ship by the Russians has long been forgotten or suppressed because of guilt feelings is false. In 1959, the sinking of the ship was immortalised in the film “Night Fell on Gotenhafen”. It is filled with German corpses and German suffering at the hands of barbarian Russians. The larger context and causes of the suffering are ignored.

Rather than a repressed silence about German suffering in the years following the war, there is almost nothing else in the media coverage of the early post-war decades.

Mark Wolfgram
Carleton University
Hull, Canada

SIR – Though the Germans have admirably owned up to crimes against the Jews under Nazism, what remains hidden from the German public is the damage done by the Nazi war machine (and its aftermath) to the non-Jewish populations of neighbouring lands. For instance, many Germans are unaware that millions of Poles were uprooted and dispossessed by the boundary realignments after the war, or that the depredations of the Red Army were not limited to Germans as they swept through Central European countries “liberating” them.

As for the Dresden tragedy, among the civilian casualties was a large forced-labour population. Their existence is rarely mentioned because the issue of just how widespread slavery was in Germany at that time has remained taboo.

J.N. Stroyar
Frankfurt

Dry land

SIR – You claim that Australia is the world's driest continent (“The parched earth”, November 23rd). This would only be true if it were to have the least precipitation, which it does not. Surprisingly, Antarctica is the world's driest continent; Australia comes second.

Juergen Koller
Erding, Germany

The bear facts

SIR – You forget a key member of the marketplace fauna; wily investors (“You beasts”, November 23rd).

It is abundantly clear that they should be called coyotes. The coyote is able to fill every niche left after the destruction of sheep, turkeys, lemmings, snakes, etc.

James Lipton
Sharon, Connecticut

SIR – When asked to what he attributed his success buying and selling shares, Bernard Baruch, the famous financier and presidential adviser, is said to have replied, in his notoriously thick accent: “Buy sheep and sell deer.”

Gunter Rischer
Nice

SIR – Bulls throw their victims up; bears throw their victims down.

Robert Race
Geneva

SIR – Your piece on bears neglects to mention the fundamental truism that, “Some days you get the bear and some days the bear gets you.”

Conrad Bona
London

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The economy

We will never surrender

Dec 5th 2002 | WASHINGTON, DC
From The Economist print edition

AP

Is America's remarkably resilient economy over the worst?

Get article background

NEVER in the field of human commerce have so many spent so much on so little—and then wondered whether he will really like it. America's holiday shopping season began in spectacular style last week. On November 29th, the day after Thanksgiving, Wal-Mart, the country's retail giant, took in $1.4 billion at its tills—a 14% rise over 2001 and the firm's biggest one-day taking ever. According to a survey by the National Retail Federation, three out of every four consumers were out shopping last weekend—and they appeared to be spending freely. Sales for the weekend were running 12% above last year, according to ShopperTrak RCT, a firm that collates data from thousands of shops.

Festive logistics partly explains this spending fervour. With Thanksgiving falling late, there are unusually few shopping days before Christmas this year. Large price cuts by shops also pulled in the bargain hunters. Nonetheless, a quick look at the malls hardly suggests that the great American wallet is slamming shut.

Those Thanksgiving shoppers are the latest addition to a growing body of evidence that suggests America's economy may be on the mend. Less than two months ago, the recovery appeared to have suddenly stalled. The statistics showed that unemployment claims were rising, consumer spending was falling and confidence was plummeting. A rising chorus of forecasters fretted that a return to recession (the infamous “double dip”) was imminent. The Federal Reserve admitted the economy was in a “soft spot” and cut interest rates by half a percentage point in early November.

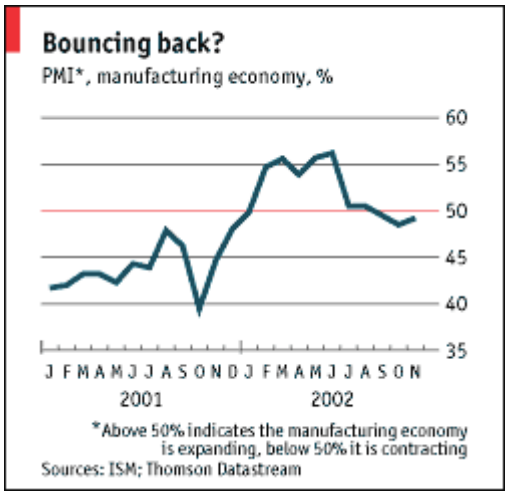
But since then a slew of statistics—from investment to productivity—have been stronger than expected, boosting the stockmarket and convincing economists that the risks of recession have receded. Stephen Roach of Morgan Stanley, perhaps Wall Street's most famous pessimist, acknowledged ruefully this week that “the second double-dip scare of 2002 now seems to be winding down.” That much is certainly true. Less obvious, however, is how strong the recovery will be.

Part of the optimism springs from hopes that business investment may finally be showing signs of life. Though overall figures on capital spending still look weak, much of the blame lies with a slump in spending on office buildings and other non-residential construction (which fell at a 20% annual rate in the third quarter of 2002). Exclude construction, and the picture becomes less dire. Overall investment in

software and equipment is rising, albeit modestly.

There are other angles from which the figures look a little better: economists at J.P. Morgan Chase point out that, if you do not include the troubled energy and aircraft industries, firms' capital spending grew at double-digit rates in the third quarter. In October, orders for capital goods outside the defence industry (and excluding aircraft again) rose by 5.5%. The question, however, is whether sustained investment growth is plausible given the substantial amounts of slack capacity that exist in many industries. Overall industrial capacity utilisation is still running at just 75%.

Look at American manufacturing directly and this mixed picture is reinforced. First came a wave of good news, particularly from the heartland, that manufacturing activity was already on the mend. The Chicago purchasing managers index startled markets on November 27th by surging from 45.9 in October to 54.3 in November. (Any reading over 50 suggests that manufacturing activity is expanding, while a reading of less than 50 suggests recession.) Unfortunately, the equivalent national numbers, released on December 2nd, showed a less perky jump from 48.5 in October to 49.2 in November, leaving it in recession for the third consecutive month (see chart). In short, American manufacturing may be on the mend, but it is far from booming.



Consumption remains the driver of any recovery. And there the good news of the past few weeks is that Americans are still spending. After falling in September, overall consumption rose 0.4% in October. Car sales, which sucked up a lot of consumer spending during the summer, did not continue their decline. Contrary to fears at the beginning of the month, a respectable number of new vehicles (16m at an annual rate) were sold in November. The Conference Board's index of consumer confidence improved during the month from a nine-year low.

A big reason for this boost in confidence, and for economists' optimism that the risks of recession have receded, comes from the job market. Judging by the fall in the weekly number of initial unemployment claims during November, the pace of lay-offs has abated. Just before Thanksgiving the number of initial claimants fell to 364,000, well below its peak rate of 433,000 in September and below the 400,000 level usually associated with an economy in recession. Though few analysts expect a sharp rise in employment (November's jobs figures are due to be released on December 6th), the fear that a sharp rise in unemployment would undermine consumption has abated.

Through the roof

Meanwhile, the housing market—another prop for consumer spending—appears brisk. Sales of existing homes rose 6.1% in October. But the signals on the market are mixed. According to the National Association of Realtors, the median home price rose 9.8% in October, the fastest rise since 1987. But the Office of Federal Housing Enterprise Oversight reckons the appreciation in house prices is beginning to stall.

High house prices are a burden for some Americans (see article); but a source of relief to many more. Either way, they surely cannot continue to soar. According to economists at Goldman Sachs the ratio of house prices to rents and income is 10-15% above its long-term average. This is a higher premium than existed at either of the two previous property-market peaks of the past 25 years.

Look at all these indicators together and the picture is one of resilience rather than strong recovery. America's economy has yet again confounded the pessimists who expected it plunge into recession, but it has yet to offer much support to the optimists who predicted strong growth. The legacy of the bubble years—slack capacity in swathes of American industry and debt-laden consumers, justifying their spending by looking at house prices—will still give the faint-hearted plenty to fret about, even as they queue up to get something for their grandparents.

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John Kerry

Where's the smile?

Dec 5th 2002 | WASHINGTON, DC
From The Economist print edition

A presidential candidate from central casting who needs to lighten up

THESE days, plenty of leading Democrats are dipping their toes in the water. John Kerry, the junior senator for Massachusetts, is wading in thigh-deep. On December 1st Mr Kerry announced that he is forming an “exploratory committee”, which is a fancy way of saying that he is running for the presidency. Two days later he travelled to Cleveland, Ohio, to outline his plans for the economy.

Mr Kerry is placing himself at the centre of the Democratic Party. In his speech in Cleveland he announced that he would roll back George Bush's plans to cut taxes by $1.35 trillion over ten years. It is unfair to give so much money back to the rich, he argued; it is also imprudent to tie the government's hands when expenditure is so unpredictable. But he eschewed traditional Democratic calls for more spending; he prefers short-term tax breaks to stimulate the economy.

He has also produced a centrist mixture of ideas on the subject he knows most about: foreign policy. He has criticised Mr Bush for letting rhetoric, as he sees it, get ahead of strategic thinking on Iraq. But he has also criticised the administration for its failure to send American troops into Tora Bora, a failure that may well have allowed Osama bin Laden to escape.

Mr Kerry's strongest card as a presidential candidate is the fact that he is a much-decorated veteran of the Vietnam war. A president who spent the Vietnam war in the Texas Air National Guard, presumably defending the Lone Star State from possible bombing by Oklahoma, can hardly impugn the patriotism of a gunboat officer. Yes, Mr Kerry voted against the first Gulf war. But he is hardly a peacenik, having supported sending troops into Bosnia, Kosovo, Panama, Somalia and Haiti.

Add to his military credentials a towering frame, an impressive head of hair, a lantern jaw and decent debating skills, and you almost have a presidential candidate from central casting. Mr Kerry nevertheless suffers from some big disadvantages.

The most obvious is that he is a Massachusetts liberal in an age where presidents tend to come from the south and the west. Mr Kerry began his political career as Michael Dukakis's lieutenant-governor, and has spent the past 18 years as Ted Kennedy's junior colleague. He has distanced himself from leftish orthodoxy on things like teacher tenure. But he rapidly retracted his criticisms of affirmative action under pressure from black groups, and he takes the Massachusetts line on gun control and the death penalty (he is for the first and against the second).

Mr Kerry's other big problem is his personality. His critics usually cite two things. The first is his upper-class background. Mr Kerry comes from a posh family (his middle name is Forbes, albeit with one “f”); and his wife, Teresa Heinz, has a personal fortune of more than $600m.

The second is unseemly ambition. As a schoolboy, he was not displeased to be called “JFK”. During the anti-Vietnam-war protests, which he joined after serving bravely in the war, he once made a public gesture of flinging his medals on the steps of the Capitol. It later turned out that he had borrowed somebody else's medals to make the gesture.

On reflection, neither of these traits seem disqualifications: politics has always been a game for self-promoters, and Americans seem to like electing toffs. Mr Kerry's real “personality problem” is that he seems so cold and aloof. His brow is perpetually furrowed. He almost never smiles. To be fair, Abraham Lincoln made rather a good president without being able to smile. But in modern times Americans have tended to like their presidents to be able to grin a bit. Can the Democrats really afford to send a dour Massachusetts liberal to do battle with an affable Texan?

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Boston's Roman Catholics

Dear Lord, can it get any worse?

Dec 5th 2002
From The Economist print edition

Yes: next, bankruptcy

Get article background

IT HAS been a fearful year for Roman Catholics in Boston. Ever more ghastly revelations of sexual abuse by priests have been followed by ever more ghastly revelations of inaction by the church hierarchy. This week the archdiocese at last released 11,000 pages of records showing that it allowed abusers to continue to work as priests well into the 1990s—long after the “reformation” of its ways that Cardinal Bernard Law claimed had taken place. Now the archdiocese may make history by declaring bankruptcy.

There is no shortage of assets. The church's property is said to be worth at least $1.3 billion, and even that figure does not take account of hundreds of acres of undeveloped land. The problem is ready cash. Charitable giving and church collections have unsurprisingly dropped, and the annual cardinal's appeal did poorly. The archdiocese has had to cut its $25m operating budget by a third, hurting poorer parishes and many church programmes. Its banks are cutting credit; its insurers are balking at paying settlements.

One charm of bankruptcy is that it would put litigation on hold. The 450 lawsuits against the archdiocese would be suspended. Thomas Bean, a local bankruptcy lawyer with Nutter, McClennen & Fish, thinks it could set a new time-frame: it would cram all the lawsuits into a single claim, limit lawyers' fees and possibly make way for a settlement fund, similar to that used by victims of asbestos.

For Cardinal Law, bankruptcy would mean no more legal predispositions where he has to answer awkward questions. But it would plainly be a humiliating first for the Catholic church, and one that the cardinal could sanction probably only with the pope's blessing. Bankruptcy would require the church to disclose its financial records to the public. And it would leave a bankruptcy judge—a layman—in charge of the church's finances.

“Canon law defers to civil law,” explains Father John Coughlin, a law professor at St John's University in New York. But there are complications. Any expenditures above $3m have to be approved by Rome. Under civil law, the property belongs to the Roman Catholic Archbishop of Boston, but under canon law it is listed as belonging to the local parishes. The diocese claims that it owns the land in trust for the parishes, so it cannot be sold off.

The cardinal is said to have hired a public-relations firm to help sell the bankruptcy idea to the public. Its efforts to do so are likely to meet much scepticism, particularly after this week's revelations about the non-reformation. The papers revealing that failure also showed that some priests were drug abusers, rapists, or had had affairs with female parishioners. Even the most dutiful Catholic may be nervous about giving money to a bankrupt entity (moral and otherwise).

The victims' lawyers argue that even talking about bankruptcy is a ploy to keep down the level of settlement pay-offs. The Dallas diocese, with the Vatican's backing, threatened bankruptcy in 1997 when it was hit by a $119m jury award to victims of sexual abuse by clerics. The victims readily agreed to a $31m award to avoid the bankruptcy courts getting involved. The Boston victims are considering walking out of the settlement negotiations.

If Cardinal Law does opt for bankruptcy, it will still be possible for the victims to sue both the cardinal and the Vatican. Whether a court can order the Holy See to cover the archdiocese's liabilities would depend on the church's corporate structure. And that, like so much else, is shrouded in the wrong sort of mystery.

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Offshore oil drilling

Plugged

Dec 5th 2002 | SAN FRANCISCO
From The Economist print edition

Oil helped California get rich. Now it makes it blush

FOR years they have been making California's greens turn purple. Two dozen oil platforms in the Santa Barbara Channel have been pumping out crude oil since the 1950s. Environmentalists—and, when it comes to offshore oil, that includes most Californians—hate them: a blowout in 1969 tarred 30 miles (48km) of coast. Hence the cheering for a unanimous judgment by the region's federal appeals court on December 2nd, which makes them the last of their kind.

The court upheld California's claim that it has the right to review 36 leases for offshore oil-exploration before the federal government extends them. The leases cover 324 square miles of ocean north of Los Angeles: crucially, they all lie more than three miles off the coast (where states have less sway than the federal government). The oil firms say there may be 1 billion barrels of oil available. But without further extensions to their leases, which California's Coastal Commission would be sure to deny, they do not have time to pump it up.

The Department of the Interior first tried to extend the leases, most of which ran out in 1999, under the Clinton administration. It argued in court that the extension of leases lay outside California's jurisdiction, since it was merely paperwork and had no direct environmental impact. Once the firms apply for the right to drill, a separate approval process would get under way, in which the state would have a say.

Greasy but natural

Oil entering North American coastal waters from:

	Tonnes '000	% of total
natural seepage	160	61.5
consumption on land, run-off	81	31.1
leaks from ships and pipelines	9	3.5
consumption at sea	3	1.1
exploration and extraction	3	1.1

Source: National Academy of Sciences

Gray Davis, the governor of California, saw no reason to wait, and plenty of votes to gain by asserting his greenery. President George Bush could still invoke the “paramount interest” of the United States to override the judgment, but that would be strange for an advocate of states' rights. Earlier this year the federal government bought out offshore leases in Florida (where Jeb Bush was up for re-election as governor) to compensate oil firms for giving up their right to drill.

Gale Norton, the secretary of the interior, has written to Mr Davis several times to propose a meeting, along with the lease-holders, to work out some such buy-out, but has had no reply. California, unlike Florida, has drawn a share of the $1.25 billion revenue from the leases, and Ms Norton would like it to help pay the firms for giving up the drilling. California, which has a $21 billion deficit, reckons it does not have to. So far the courts have backed the golden state.

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About sponsorship

Affordable housing

The roof that costs too much

Dec 5th 2002 | CHICAGO
From The Economist print edition

A problem for poorer Americans that most voters prefer to ignore

MOTHERHOOD and apple pie are still fine, but the thing many Americans relish most these days is owning their own home. Two in three homes are owned by their occupants, and the lowest mortgage rates in three decades keep the numbers rising. But this does not suit everybody.

There have long been cities, such as San Francisco and Boston, which lure in so many members of the ever-growing middle class that poorer people get priced out of the housing market. Now the problem is national. According to a report by Harvard University, house prices have been jumping ahead of incomes in most of America's big cities (see chart). Eight of the 50 biggest metropolitan areas have seen prices rise by nearly a third in real terms since 1997. The national rate for mortgage foreclosures is at a 30-year high, with Indiana, Ohio, Mississippi and Utah to the fore.

The Department of Housing and Urban Development (HUD) defines “affordable housing” as a home which costs less than 30% of a family's income, in either rent or a monthly mortgage. When households pay more than 30% they tend to skimp on other necessities, such as health care. Janet Smith, a professor of urban planning at the University of Illinois, reckons that 38% of all the renters in the Chicago area—more than 180,000 households—are in this squeeze. So are nearly a quarter of the area's home-owners. These are not just the familiar poor. A lot of teachers and nurses are struggling (see table).

Costing the earth 2

	San Francisco	Boston	Washington	San Diego	Chicago	Dallas
Apartment rent*	1,362	942	840	805	762	749
Income needed to pay rent†	54,480	37,680	33,600	32,200	30,480	29,960
Janitors' median income	20,800	20,987	15,787	16,536	18,824	14,810
Nurses' median income	39,603	39,541	33,280	31,990	31,990	38,938
Teachers' median income	38,293	38,584	32,781	38,584	36,733	34,861

*Monthly for modest two-bedroom †Assuming 30% of income is spent on housing
Source: Joint Centre for Housing Studies

Some people blame the housing burden in part for other social ills—everything from children doing badly at school to traffic-jammed roads. Unless the housing problem is addressed, claims Julia Stasch at the MacArthur Foundation, America will waste money on other social programmes.

No doubt the housing boom is unsustainable, and prices will eventually adjust themselves to incomes. But that will take time. So affordable housing has become a political issue. Mayor Thomas Menino of Boston has championed it at the Conference of Mayors, which he currently heads (but his solution is apparently to bring back rent controls, which in the end is no solution). California's voters have just approved a $2.1 billion bond issue to subsidise the provision of cheaper homes.

Such schemes usually involve cities requisitioning land—often run-down areas where factories or public-

housing developments once stood—and handing it over to housing associations or public trusts which, because they get the land cheap, can build homes and rent them out at below-market rates. The trouble is that demand generally swamps supply: in cities like Washington, DC, there have been complaints of Soviet-length waiting lists. The obvious way to mop up some of the demand—more high-rise, high-density apartment blocks—is opposed by people who own houses nearby; many neighbourhoods have zoning laws to prevent this.

Another problem is that few countries offer such generous tax breaks to home-owners as America does. The Chicago area's population has increased by 11% since 1990, according to Ms Smith; but the number of rented homes has dropped by 3%. Jim Houlihan, the Cook County assessor, successfully pushed for lower taxes on rented property. Unfortunately, most of the city's new jobs are in its northern suburbs, which are protected by zoning laws; most of its cheaper housing is in the south. If people live a long way from their work, business suffers, the transport system creaks, and the environment (think of those car fumes) takes a beating.

An organisation called Metropolis 2020 estimates that the Chicago area will need another 352,000 homes by 2020. But many neighbourhoods are suspicious of anything labelled “affordable housing”, often assuming that it means public housing (which they rightly or wrongly associate with racial minorities, drugs, gangs and violence). It is true that cheap housing projects do tend to be built in poorer areas. One of the biggest in the country is a $1.6 billion scheme in Chicago: the city is knocking down some of its nastiest public-housing projects, including the notorious Cabrini Green. But the 25,000 new units it is building in their place are divided between public housing, subsidised homes and market-rate ones.

Some people argue that the federal government should step in—by creating a National Housing Trust Fund to help build cheaper homes; by altering the tax system; by making the Federal Housing Association more efficient. But HUD's boss, Mel Martinez, has told the mayors that “the solution will not come out of Washington”. He wants the private sector and non-profit organisations to take the lead.

In the end, it may be true that the only answer is to allow the building, or renovation, of a lot more cheap housing. But many middle-class voters do not want that in their communities. “Most Americans don't think there's a housing problem,” says Nicolas Retsinas of Harvard. Most homeowners are still happy with rising prices. Affluent baby-boomers will probably ignore the problem until their children decide that it is cheaper to stay with mum and dad than pay a fortune for their own homes. And by then the property market will doubtless have crashed.

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Lexington

Beware the K-Street conservatives

Dec 5th 2002
From The Economist print edition

The only people who could stop a Bush second term

NEVER underestimate George Bush's ambition. Back when he was a mere shrub in Texas he succeeded in turning a small victory in his first race for governor into a resounding triumph in his second. Now he is well on the way to doing exactly the same thing on a national scale. Work is well advanced on both next year's budget and his state-of-the-union address. The president's staff are casting around for a big idea to galvanise his domestic agenda for the next couple of years—perhaps even adding individual-investment accounts to Social Security.

The Republican Party now thinks it is close to replacing the Democrats as America's majority party. In 2004, the talk is not just of a second term for Mr Bush but of expanding the party's majority in the Senate (the Democrats are defending more vulnerable seats). Some obvious things could still get in the way: a disastrous war in Iraq, or a severe downturn in the economy. But a more subtle threat could come from the party's business wing.

How could business be a problem? The president has hardly made a secret of his belief that the business of America is business. He stuffed his cabinet with the sort of people whose first reaction to news of some tycoon's obscene retirement package is to wonder why they hadn't fixed so luscious a deal for themselves. Mr Bush spent his first two years in office delivering tax cuts and “regulatory roll-back” to the industry lobbyists who hang their hats in Washington's K Street.

And isn't the lesson of Enron that Mr Bush is immune from corporate scandals? The oil-and-gas company sprang from the heart of Bush country. “Kenny Boy” Lay was a close personal friend of the Bushes, and his minions played a leading role in designing the administration's energy policy. The public's reaction to the infamous corporate scandal that hastened the stockmarket's collapse? They exempted Mr Bush from blame, and voted for Republicans the first chance they got.

But K Street could nevertheless end up hurting Mr Bush with the K-Mart crowd. The most obvious problem is the growing temptation to over-reach. The trouble with lobbyists is that their appetite only grows with the eating—as anyone who visits Morton's steak-house or any of the other temples to gluttony around K Street can testify. The Republicans celebrated last month's triumph by fast-tracking several K-Street favourites: exempting older coal-fired plants from new anti-pollution rules, and making it easier to open national forests to logging and drilling.

The lobbyists' biggest coup has been the revision of the Homeland Security Bill. One new provision allows companies that have registered overseas to escape American taxes when they get contracts with the

department. A second provision frees companies that make faulty anti-terrorism equipment (such as bomb detectors and gas masks) from liability to prosecution. A third restricts the liability of drug companies that produce smallpox vaccines. A fourth tries to shield Eli Lilly from lawsuits seeking billions of dollars for families of autistic children. And there is more of this sort of stuff to come. Last month the lords of the pharmaceutical industry—who spent $35m on the two most recent elections—went into a huddle to plan their next demand.

Now, some of these things are more nuanced than they appear; and a few other corporate lobbying campaigns, such as the one for a simpler tax code, may even be downright healthy. But in politics appearances count, and this sort of thing spells danger for a president who is reaching out to voters of the middle ground. Most swing voters, particularly women, put the environment high on their list of concerns. And Mr Bush surely needs to be holier than the pope on security issues. It is hard to ask Americans to make sacrifices for the sake of national security if you are handing contracts to companies that refuse to pay taxes. And it is a bit rich to claim that defence is your over-riding priority if you apparently let your fellow Republicans doctor the Homeland Security Bill for the benefit of a big drug firm.

But the biggest problem with K-Street conservatism is that it puts producers in front of everybody else. There was a time when conservative Washington was full of Adam Smith enthusiasts who solemnly intoned that good government must promote competition, not hand out favours to cronies. But most of those young Reaganauts have long since taken the lobbying industry's dollar. Now the talk is of commerce, not competition.

The Republicans' incestuous relationship with the business establishment has blunted its enthusiasm for corporate reform. The collapse of Enron and WorldCom revealed serious structural problems: too much power for imperial executives, too few independent directors, too little concern for shareholders' rights. But the White House still seems to think that the scandals were about a few bad apples rather than rotten branches and roots.

K Street v K-Mart

Mr Bush has proved remarkably adept at dumping his business cronies when they become bothersome: Kenny Boy rapidly became Ken Who? But so far the only restraining order the Republicans have put on K Street has to do with money. Tom DeLay and Trent Lott, the heads of the House and the Senate, have told lobbyists to stop dividing their largesse between the two parties; now the Republicans should get 90% of the pot.

So far the Democratic Party has been startlingly inept at making an issue of Mr Bush's corporate connections. But you cannot build an enduring Republican majority on the assumption that the other side will remain incompetent for ever. Mr Bush should remember that even Al Gore, perhaps the most unattractive presidential candidate since Richard Nixon, managed to win 51m votes with a populist campaign that pitted the people against the powerful. It is by no means impossible that a more attractive populist, perhaps North Carolina's John Edwards, may still be able to twist K Street conservatism into a winning issue.

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Venezuela

When push comes to shove

Dec 5th 2002 | CARACAS
From The Economist print edition

AP

Once again, oil workers are joining a general strike. Will the army follow?

Get article background

OUTSIDE an office building in eastern Caracas belonging to the state oil corporation, Petroleos de Venezuela (PDVSA), is a small patch of grass with a flagpole and a plaque. The plaque commemorates "the actions of those who defended with passion the principles and values that sustain the national oil industry", the mainstay of the country's economy.

This is "Meritocracy Plaza". Its name commemorates the *casus belli* of the oil strike of April this year, when managers and workers alike objected to President Hugo Chavez's placing of his own men on the board of PDVSA. That stoppage led within a week to the president's temporary removal from office, after 19 demonstrators died and the armed forces ceased to support him.

The events of April underscored that if the president wished to cut short his political life, he had only to alienate oil workers and the armed forces, preferably simultaneously. But the real question is whether those who have little or no faith in Mr Chavez will dare to stand up to him.

Tuesday, December 3rd was the second day of Venezuela's fourth general strike in 12 months. As usual, the strike was only a partial success. Its formal aim was to persuade Mr Chavez to agree to early elections in some form, as a means of resolving peacefully the bitter political conflict that has polarised the country. The president has ruled out anything sooner than a recall referendum late next year.

The opposition, however, seemed to have painted itself into a corner. Pressure from below, combined with the president's provocative behaviour (such as attempting to seize control of the Caracas police force), pushed it to strike at a bad time. Shopkeepers hardly want to close their doors in December, just before the Christmas boom. The oil industry, with no big internal ructions going on this time, at first joined in only slowly. The government, it seemed, could sit back in relative comfort and wait for the strike to crumble.

Then, in the early hours of Tuesday, armed men broke into the house of Juan Fernandez, the best-known of the PDVSA management dissidents. They held him and one of his daughters at gunpoint, robbed him and told him, he says, "that they had been sent to kill me." Not unnaturally, Mr Fernandez and his fellow

dissidents called an open-air meeting in Meritocracy Plaza to protest.

A few hundred peaceful demonstrators, including children, heard the oil managers give some rather inflated figures about the impact of the strike on fuel supplies. They waved their flags, blew their whistles and chanted. And then along came a National Guard riot squad, equipped with quantities of tear-gas which they dispensed without warning. Journalists who asked questions were gassed, shot at with plastic bullets and hit with the flat edge of the blunt swords the guardsmen carry. And in a trice the strike organisers had the momentum—and the excuse—to extend the strike for another day and call street demonstrations.

Some opposition radicals blocked the nearby motorway and set fire to a dust-cart. The National Guard brought out its armoured cars and fired more gas and plastic bullets before being suddenly, and inexplicably, withdrawn. Meanwhile, hard-line leaders of the president's Fifth Republic Movement (MVR) made back-to-back speeches on state TV, arguing that the assault on Mr Fernandez was a put-up job and that the opposition was implementing a “terrorist plan” to overthrow the government with support from abroad.

When asked why the National Guard had used disproportionate force, Mr Chavez said such decisions were taken at “another level”. The government's pretext was that the PDVSA building lies inside one of eight “security zones” in the capital, where demonstrations require permission from the defence ministry. The opposition regards the zones as illegal and unconstitutional, and the government has sometimes chosen not to enforce them.

It was hard to avoid the conclusion that Mr Chavez, once again, was pushing the opposition into a confrontation. If the strike becomes indefinite, the president can more easily dismiss its organisers as “fascists, terrorists and coup-plotters”, representing “minority groups”. As Wednesday turned into Thursday, tanker loadings were increasingly delayed and, on one company tanker, the crew refused to let the vessel proceed. But the unknown factor, as ever, remained the armed forces. The logic of confrontation implied an escalation of violence. Just how far along that road the military men would accompany the president was anyone's guess.

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Colombia

An olive branch of sorts

Dec 5th 2002 | BOGOTA
From The Economist print edition

When a ceasefire is offered by an outlaw, can he be believed?

Get article background

Reuters

If Castaño behaves, perhaps they won't extradite him

HE IS a self-confessed murderer, a fugitive and the figurehead of the country's vicious paramilitary groups. Yet Carlos Castaño has offered an olive branch to his country: an indefinite unilateral ceasefire by his factions, which began on December 1st.

Not so long ago Mr Castaño was promising that his United Self-Defence Forces of Colombia (AUC), which have grown rapidly over the past decade and number around 8,000-10,000, would never lay down their arms until Colombia's left-wing guerrilla armies, the ELN and the FARC, did the same. The paramilitaries fight both these groups, often with low-level co-operation from Colombia's legitimate armed forces. Now the AUC says it wants immediate dialogue, crop-substitution programmes to curb cocaine production, and even such sugary gestures as a handover to UNICEF of child combatants.

This offer has come about after secret contacts, mediated by Catholic bishops, with President Alvaro Uribe's government. Unlike his predecessor Andres Pastrana, whose peace efforts took place in front of the television cameras, Mr Uribe has proceeded extremely quietly in all contacts with the country's powerful illegal factions. With the 18,000-strong FARC, he has admitted that he would like some kind of humanitarian exchange to free the guerrillas' kidnap victims. With the 5,000-strong ELN, the weakest of the armed groups, contacts continue in Cuba. But the offer from the AUC is the most eye-catching and concrete so far.

Previous governments have been unwilling to grant any kind of political status to Mr Castaño and his sort. But the AUC's military and financial might—it is financed in large part by drug trafficking—give it de facto political power, and Colombia's congress has also removed rules that limited negotiations to official political bodies. Mr Uribe has said he will not talk to any armed group until hostilities cease. So far, though, his government has given no public response to the AUC ceasefire.

Why the AUC's change of heart? Mr Castaño, a relentless self-publicist in recent years, has often outlined a vision of his future as a non-outlaw. This year he stepped aside from the AUC's military leadership, at least nominally, and appeared to push the group towards a break with drug-trafficking. In September, the United States demanded his extradition on cocaine-trafficking charges. By seeking a ceasefire, the AUC is hoping Mr Uribe will suspend legal action against its leaders, as Mr Pastrana did for FARC leaders during their failed peace talks.

Colin Powell, the American secretary of state, who visited Mr Uribe on December 4th, says the United States is waiting to see whether the AUC—listed in Washington as a proscribed terrorist group—really begins to talk seriously about disarmament. In any case, much ground needs covering before negotiations could begin. It is not clear how the government could finance the disarming and retraining of AUC soldiers, unless it were to press many combatants—some of them of proven brutality—into legitimate military service. The state could not fill the vacuum in areas the AUC claims to have “liberated”. And many splinter paramilitary groups would love to take over the drug-smuggling business and the black market for petrol. Even if the AUC offer proves serious, it will be only one step towards curing Colombia's ills.

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Mexico's budget

No trolley needed

Dec 5th 2002 | MEXICO CITY
From The Economist print edition

Just a fairly large pocket

THE Mexican government's budget proposals for 2003 are now going through Congress. Nothing very unusual about that: except that, by comparison with previous budgets, this one has shrunk—by about one foot and ten inches, or 56cm. Mexico's legislators now have a handy, 450-page single-volume summary of the budget to consult, containing a crisp synopsis of each department's aims, main spending plans and performance targets.

The budget used to come in only one format: multiple volumes. The 2002 budget, considered slim at the time, took up two feet of shelf space, not counting three boxes of supplements. Congressmen were given their own trolleys to cart the thing around.

There was a point to the old budget format, of course. Javier Bonilla of Quantica, an economic consultancy, describes the old system as a “strategy of disinformation by volume”. Since few legislators could take the time to read it, and even fewer could understand it, governments could avoid financial scrutiny.

In any case, like the old Soviet budgets, few congressmen doubted that the whole thing was mostly fiction anyway. Large parts may still be; but the new budget format has nonetheless been welcomed as a small but significant part of President Vicente Fox's drive to make Mexico more modern.

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Canadian health care

Prescription for change

Dec 5th 2002 | KITCHENER-WATERLOO, ONTARIO
From The Economist print edition

Is Roy Romanow's report what Canada needs?

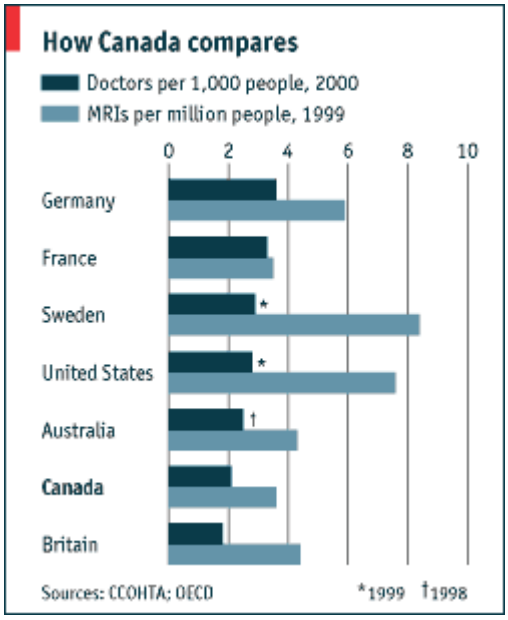
AROUND 300,000 people live in Kitchener-Waterloo, a fast-growing city bustling with insurance companies and IT firms. The city's central hospitals reflect this growth, with new facilities springing up for cancer and cardiac care. But hospital administrators have many worries: tight budgets, too few doctors, rising drug costs, and long waiting times for elective treatment and sophisticated diagnostic tests.

Such concerns are heard across the country. Canada's health-care system is not yet at breaking point like Britain's National Health Service, nor does it have America's runaway medical inflation and millions of uninsured. But Canadians worry that their taxation-based, “single payer” system will not be able to deliver good care for all who need it in future.

This week, politicians were busy mulling over “Building on Values: The Future of Canada's Health Care System”, the final analysis and recommendations of Roy Romanow, Canada's one-man health-care commission, who was appointed by the prime minister last year. Roughly C$15m ($10m) later, Mr Romanow has concluded that both the health of Canadians and their medical system compare favourably with other countries, but that more money, and considerable structural change, are required to make the most of changes in modern medicine and to level the playing field between Canada's richest and poorest provinces.

Although “medically necessary” hospital care and physician services are paid for by the state, more than a quarter of all health-care spending in Canada—for such things as out-patient prescription drugs and home care after hospital—comes from private pockets. Mr Romanow wants to change this, and has suggested bringing some forms of home care under the public umbrella. He also suggests the payment of a C$1 billion-a-year transfer to help Canadians pay for “catastrophic” drug expenses, as well as extra money to boost access to health care in rural areas, reform the delivery of primary care and improve the provision of fancy diagnostics such as MRI scanners (see chart). Mr Romanow recommends a more systematic approach to organising waiting lists, as well as the creation of a national Health Council to monitor the performance of the system and sort out the staffing problems.

All this, he reckons, will require a rise in federal funding from around C$8 billion today to roughly C$15 billion by 2006. This would raise the federal share of spending to 25% after years of decline, which left the hard-pressed and increasingly grumpy provincial governments to pick up the bill. But it is not clear how much the federal government will agree to provide.



The prime minister, Jean Chrétien, has called a meeting of provincial premiers for January to thrash out what to do about the report. It is likely to be a noisy affair. Ontario, Alberta and Quebec are already unhappy. Conservative critics, such as Stephen Harper, the leader of the Canadian Alliance party, have lambasted the report for rejecting a greater role for private health care. Mr Romanow sees little benefit either in more private spending on medicine, or in private for-profit provision of care.

Despite this, several provinces, notably Alberta, are already pushing ahead with for-profit diagnostic centres and clinics. Getting them to toe the Romanow line will not be easy. But as Raisa Deber, a health-policy expert at the University of Toronto,

points out, the strongest selling-point of Mr Romanow's report is not his largely sensible proposals, but the fact that he spent 18 months listening to the views of ordinary Canadians. Politicians may not like what he has to say, but public pressure will ensure they listen closely.

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Brazilian politics

The fun stops here

Dec 5th 2002 | RIO DE JANEIRO
From The Economist print edition

Political scrapping, and inflation, rear their heads again

EPA

Can I be in your cabinet?

FOR Luiz Inácio “Lula” da Silva, these have been glorious days. He disburses autographs, blows kisses from balconies, and drives his bodyguards to despair as he plunges into one adoring crowd after another. And why not? Just the other day, this woolly leftist was the nightmare of the financial world. Now the Brazilian currency and bonds have rallied, and talk of imminent debt default has faded.

Yet the fun won't last. Well before he takes over on January 1st, Lula is feeling the weight of office. Electoral allies are snarling over plum cabinet jobs, unions are pushing for a hefty minimum-wage increase, and state governors are clamouring for debt relief. Worse, inflation is back. Consumer prices are rising by 10% a year, the worst rate since 1994.

Perhaps to prolong his brief honeymoon, Lula has hit the road. In his first official excursion as president-elect, he swung through Argentina and Chile early this week and will call on Mexico next. These are friendly nations with which Brazil has long enjoyed cordial if drowsy relations. Lula wants to perk things up by reviving Mercosur, the ailing South American trade association that nearly collapsed under the dead weight of the Argentine economy. He will end up in Washington, where he may have to answer questions about his repeated blasting of America's efforts to create a pan-American free-trade area as “annexation”.

Lula must patch together a broad ruling coalition

Meanwhile, he has been very slow to name his cabinet. The task is not easy. With the PT controlling just 18% of Congress, Lula must patch together a broad ruling coalition. Every invitation to join the cabinet is also a snub, and every snub a potential defection. “Assembling the Brazilian ministry is one of the most delicate tasks of political engineering there is,” says Mailson da Nobrega, a former Brazilian finance minister. But for all the intrigue, most of the top jobs are likely to go to PT potentates, who could get the nod by this weekend. The Central Bank post may take longer, and will almost certainly fall to a man with proper market-friendly credentials. Lula has made it clear that he does not want Arminio Fraga to stay.

Jose Dirceu, the PT president, is likely to be Lula's chief of staff. As a former student rebel, he spent part of the 1970s exiled in Cuba and the rest living clandestinely in Brazil (thanks to a facelift and a spook's discretion) until a political amnesty was declared in 1979. He fixed his face, dumped his wife and child, and plunged back into politics. He helped found the PT in 1980, and then, when things went awry, set out to reinvent it, reaching out to the business community and muscling the party *militantes* into the political middle.

The top tip for the finance ministry is Antonio Palocci, the youngish former mayor of a city in Sao Paulo's farm belt, who now heads the transition team. Mr Palocci is big, amiable, whiskered, and like Lula speaks with a disarming lisp. But he has won praise for his prescriptions for Brazil's economy: low inflation and a hefty primary budget surplus for now and, in time, reform of taxes, labour laws and the money-losing pension system. “The Brazilian economy is a ship, not a speedboat,” he said last week. “We can't expect any abrupt turns.” For a country still struggling for ballast in the world markets, that may be just the right course.

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China and North Korea

Report from the icy frontier

Dec 5th 2002 | TUMEN, YANBIAN PREFECTURE
From The Economist print edition

James Miles

Why the Chinese will not destabilise their troublesome neighbour

Get article background

IN A few days' time, the ice on the Tumen River dividing China from North Korea will thicken into a hard crust. For starving inhabitants of North Korea, this would normally be a good time to start making preparations to escape. A few easy steps across the poorly guarded and frozen border and they would have a chance of finding work that could fill their stomachs. But, fearful that the flow of migrants could become a torrent, China is no longer turning a blind eye to the refugees who once easily blended into the large community of ethnic Koreans on its side of the narrow river.

As the world wonders how to respond to North Korea's admission that it is enriching uranium (which can then be used to make nuclear weapons), China's worries about refugees act as a brake on any plan that might destabilise its neighbour. From China's point of view, it is better to preserve North Korea's few remaining economic lifelines than risk nudging Kim Jong Il's regime towards an implosion that could send millions pouring across the Chinese border. Perhaps even worse, as China sees it, the vacuum created by such a collapse might draw American troops and their South Korean allies into a disintegrating North Korea, right up to its border with China. Better to maintain the status quo than bring China's biggest potential enemy to its doorstep.

How effective economic pressure on North Korea would be is debatable. The Korean Workers' Party remained firmly in control through a famine lasting several years after 1996 that left many thousands dead. Thanks to foreign assistance and better weather conditions, food production and supplies have somewhat improved. But industry remains in tatters and there is no sign that the party's grip has weakened in the slightest. The tiny number who dare to dissent are imprisoned or, sometimes, executed in public.

What is certain is that no economic sanctions would work without the help of China, North Korea's main provider of fuel and food aid. Tim Savage, at Kyungnam University in Seoul, estimates that, since last month's suspension of American heavy fuel-oil supplies to North Korea, China provides 70% of the North's oil. He says this is used mainly by the armed forces and for transport. A study published last year by Yanbian University predicted that China

would remain the biggest supplier of food to make up the shortfall between North Korea's grain production and its minimum needs (the World Food Programme estimates the shortfall will be 1.1m tonnes next year, compared with 1.3m tonnes this year). Western countries and South Korea are also contributors.

China is worried that a nuclear-armed North Korea might lead Japan to go nuclear, too. But it is hoping that, so long as Japan's alliance with America remains strong (and the status quo on the Korean peninsula will help it to remain so), a nuclear break-out by Japan is unlikely. So China wants to maintain North Korea's stability in order to preserve its own.

In Yanbian prefecture, the first port of call for most of the North Koreans trying to escape from their country, this concern is clear in the way refugees are being handled. For years, severe penalties imposed by the North Koreans on those trying to escape kept the numbers crossing the river at manageable levels. Chinese officials often did little to prevent people crossing into Yanbian, 40% of whose population is ethnic Korean. But in the past few months foreign activists have been helping refugees to enter diplomatic missions in Beijing and other Chinese cities to claim asylum. Their aim was partly to force China, which would have to approve the asylum-seekers' departure to third countries, to recognise them officially as refugees.

This has backfired. China has allowed 100 or so North Koreans who made it into foreign missions to leave for South Korea. But to discourage others from making similar attempts, it has erected barbed wire around embassies in Beijing and has more than doubled the number of guards around them. It has also launched the biggest round-up of North Koreans in the border area in recent years, and has imposed tough penalties on those who help them. People in Yanbian say fewer Koreans are trying to cross the river. The influx between December and February, when the average temperature is more than ten degrees Celsius below freezing, is likely to be far less than usual.

In the past, North Koreans who made it across would often head for Christian churches, which would give them food and money. Friendly foreigners would help some of them try to escape to South Korea via Mongolia or through South-East Asian countries. But now church workers say that even giving food to a North Korean can incur a fine of 5,000 yuan ($600), about six months' wages for the average worker in a state-owned enterprise.

The police encourage suspicion among refugees and their helpers by offering some captured North Koreans the chance to stay in China if they reveal the whereabouts of compatriots in hiding. Members of foreign non-governmental organisations trying to help the refugees have been fined and sometimes detained or expelled.

The police now regularly enter villages near the border to check the identities of inhabitants and stop vehicles that might be carrying North Koreans. In Tumen, a town that has become a major border crossing-point, North Koreans are frequently escorted back by Chinese police.

The odd thing is that local people say North Korea's treatment of those sent back is less tough than it was a few years ago, when many were imprisoned and tortured and some were killed (though Human Rights Watch, an American group, reported in November that there were signs that their treatment had begun to worsen again this year). The lucky ones are kept in detention for a few days or weeks before being released, a process than can be expedited with bribes of money or food. But members of the ruling party, and people in politically sensitive jobs, can still expect far worse treatment.

Estimates of how many have made it into China in recent years vary widely. The figure often cited by human-rights groups is 300,000. Some diplomats prefer a figure in the tens of thousands.

Until the recent crackdown, many of those who crossed into China returned with food for their families. But there is little doubt that if China and North Korea were to get more relaxed over cross-border movements, the number trying to escape once and for all would jump dramatically. An American Korean in Yanbian, who is a regular visitor to North Korea, says that he was once told by a senior North Korean official, with no visible curve of the lips, that, if his compatriots were allowed to leave freely, there would soon be only one person left in the country: Kim Jong Il.

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China, Russia and North Korea

A friendly word

Dec 5th 2002
From The Economist print edition

But will North Korea give up its bombs?

Get article background

Reuters

It's time

EAST ASIA is the place where China, Russia and the United States bang elbows with each other. But a joint statement issued this week by China's president, Jiang Zemin, and his visiting Russian counterpart, Vladimir Putin, for the first time publicly backed up America in its efforts to press North Korea to abandon its secretive nuclear-weapons programme. It was “crucial to peace and security in north-east Asia”, the two leaders said, “to maintain a nuclear-free Korean peninsula and the system of non-proliferation of weapons of mass destruction.” As Russia did after the September 11th terrorist attacks on America, it seems that China has seen the value of co-operation in the face of new dangers.

Since the early 1990s, when North Korea was first fingered by the International Atomic Energy Agency (IAEA) for producing more bomb-usable plutonium than it had owned up to, China has resisted applying any sort of pressure on its sort-of-friend to give up its weapons-tinkering. Indeed, both China and Russia have helped North Korea with missile and nuclear technology. Weapons proliferation—including the North's missile sales to unstable regions—was seen as damaging only to western interests, particularly America's.

That view was always short-sighted. North Korea's recent admission that it is pursuing another route to a bomb—this time by enriching uranium—has brought home the problem to China in more ways than one.

North Korea's test of a rocket over Japan in 1998 had already undercut China's efforts to persuade the Japanese not to take part in missile-defence work with America. China worries that the uranium confession could eventually encourage Japan, South Korea and even Taiwan to think of getting such weapons. And, since North Korea got its start in the uranium business from Pakistan, which has also had both nuclear and missile help from China, that makes China a victim of its own past rule-breaking.

Teaming up with America, South Korea and Japan in pressing North Korea to give up its nuclear ambitions now seems more prudent. A 1994 deal negotiated by America that froze North Korea's plutonium production in return for oil deliveries and the building of two less proliferation-prone nuclear reactors hangs by a thread. America and its allies have suspended oil shipments and next week will discuss whether to halt the reactor construction too. China and Russia want both sides to keep to the 1994 agreement and others that ban nuclear weapons from the peninsula, and on that basis to open talks.

This would entail North Korea's verifiably dismantling its uranium programme. The IAEA stands ready to do the verifying. Will North Korea oblige?

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Indian democracy

State of concern

Dec 5th 2002 | AHMEDABAD
From The Economist print edition

Gujarat's voters could decide the future of the whole country's government

Get article background

FOR two years the state of Gujarat in western India has been making unhappy headlines: it has suffered an earthquake in January 2001 in which some 40,000 people died; the worst drought in a decade; and, earlier this year, murderous communal violence. Now an election on December 12th for the state's legislature will have nationwide repercussions. Gujarat is back on the front pages. Once again, it is not a good-news story.

For that, blame Narendra Modi, the acting chief minister. Mr Modi, from the Hindu-nationalist Bharatiya Janata Party (BJP), which leads India's coalition government, is exploiting communal tensions for hoped-for electoral gain. If he succeeds, the habit may catch on. It could poison Indian politics before the general election that is due by 2004 at the latest, and raise questions about the future of the prime minister, Atal Behari Vajpayee, a BJP moderate. If he fails, the BJP-led government will be weakened, perhaps terminally. Some political observers reckon that Gujarat's is the most important state election for a decade.

Long a controversial figure, Mr Modi has been pilloried for his role in the riots that scarred Gujarat after February 27th. That was when a carriage on a train bringing Hindu activists back from the site of a contentious proposed temple in Ayodhya was set on fire in the town of Godhra. Fifty-eight people, mostly women and children, were killed.

There followed, in parts of Gujarat, a pogrom against Muslims. More than 2,000 people died. Mr Modi's government is accused, at best, of having failed to stop the bloodshed; at worst, in a report of a recent investigation, of taking a part in leading and sponsoring the violence.

The state government's alleged motive was electoral. In 1998, the BJP won 117 out of 182 seats in the state legislature with 45% of the vote. But because of its poor performance in office it was losing by-elections to the Congress party, which also forms the main national opposition.

Congress could attract the votes of Muslims (some 10% of the population), of other minorities, such as tribal groups, and of lower-caste Hindus and Dalits (formerly “untouchables”). But if the 30m-strong electorate votes on communal Hindu v Muslim grounds rather than for caste or economic reasons, it would benefit the BJP. The violence, much of which pitted Dalits against Muslims, made this more likely.

In July Mr Modi called an early election. This attempt to capitalise on the communal tension was thwarted, however, by India's independent election commission, which delayed the poll until tempers had cooled. Mr Modi has railed against the election commissioner, J.M. Lyngdoh, joking that he may be Italian (like Sonia Gandhi, Congress's leader, who launched her party's campaign this week with an address to a huge public rally). Now, opinion polls in what seems to be a close contest are divided on whether the Hindu card is proving a trump or not.

The Congress party in Gujarat is led by Shankersinh Vaghele, who himself comes from the Hindu nationalist movement. He says that his party's campaign will take up issues such as the shortages of electricity and drinking water in the state, and adds that the main theme of the election is the caste of the candidate, rather than the communal divide.

Mr Vajpayee has said that the Godhra massacre should not be an election issue. The BJP manifesto is dutifully silent. But posters of Mr Modi, defiantly silhouetted against the backdrop of a blazing train, have

appeared across Gujarat. The BJP's sister organisations, such as the World Hindu Council (the Vishwa Hindu Parishad, or VHP), have shown little restraint.

Prawin Togadia, the VHP's international general secretary, says people need to be reminded of Godhra and the threat to Indian civilisation posed by Islamic fundamentalism. Gujarat, he points out, borders on Pakistan, and he alleges that it is Pakistan's next target after Kashmir, where India accuses it of waging a proxy war of terrorism. Mr Togadia says he is on the front line: his own life has often been threatened. On December 3rd, a local leader of the VHP, Jaideep Patel, was shot and wounded on the outskirts of Ahmedabad, the state's largest city.

He insists that he and Mr Modi both stand for a version of Hindutva, a nationalist creed, that is pluralist, inclusive, democratic and secular. These are the foundations on which independent India's founders sought to build their state. But Gujarat is regarded as a laboratory for Hindutva. It would not just be some upper-class liberals who would see a decisive victory there for Mr Modi as a potentially explosive threat to that underpinning.

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Press freedom

The Economist's award

Dec 5th 2002
From The Economist print edition

The courage of a journalist in Kazakhstan

Get article background

THOUGH often despised in the free world, journalists there suffer none of the dangers that afflict their counterparts in many unfree countries, where their work may be even more valuable. One such country is Kazakhstan, once part of the Soviet Union and run by the increasingly despotic President Nursultan Nazarbaev. And one journalist—among others—who has defied his intimidation is Lira Baysetova, the owner and editor of an investigative opposition newspaper, *Respublika 2000*, until it was shut down by the government in February. Four months later, her 25-year-old daughter died in mysterious circumstances in police custody. By giving her its annual Freedom of the Press Award this year, *The Economist* has recognised Mrs Baysetova's courage, in the hope that it will inspire journalists both in Kazakhstan and elsewhere.

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Afghanistan, one year on

Happy anniversary

Dec 5th 2002
From The Economist print edition

The slow path to stability

ONE year after drafting in Bonn a plan for the future of a post-Taliban Afghanistan, its main architects got together again on December 2nd to reflect on how far the country had progressed. They had reason to pat themselves, and the Afghan government, on the back. For the first time in over two decades, Afghanistan is not at war; the Taliban and their al-Qaeda protégés are no longer organised forces; a transitional government was elected in June; a flurry of groups are at work on human rights, legal reform and the constitution; foreign countries have promised over $5 billion in aid over the next five years and maintain an International Security Assistance Force (ISAF) to help secure Kabul; 3m children (including 1m girls) are at school; and almost 2m refugees have come home.

But Afghanistan is hardly a haven of peace and stability. Al-Qaeda and the Taliban can still create instability by terrorist attacks. In addition, *mujahideen* once united by their struggle against Soviet occupation, and then against the Taliban, are fighting each other in some areas. On December 1st warlords clashed near the air base of Shindand in western Afghanistan, and an American B-52 dropped bombs after coalition troops came under fire. This was the first time in months that American aircraft have been in combat.

The mandate of ISAF has been extended for a year, but its reach has not. Some American soldiers will be deployed in provincial cities to help with reconstruction. The Americans try to keep clear of local feuds, but may have to intervene again when caught in crossfire.

The central government still has few tools to establish its authority. International donors are helping to create a national army and police force, but it will be years before they can really control the country. On December 1st President Hamid Karzai issued a decree that outlaws any military force other than the army. But it is little more than a declaration of intention. Nor does it offer much of a carrot. Warlords generate their own revenues by collecting taxes and duties on trade—and, in some areas, through opium trafficking.

The government has little income of its own. Afghans complain that the most visible sign of foreign aid is aid workers driving spotless land-cruisers in Kabul, not tangible improvements in the life of the local people. Of the $1.9 billion promised for reconstruction this year, two-thirds has come available, but only a tenth has so far gone to the government itself. About two-thirds of the money is being spent on such necessities as food and helping refugees, not on longer-term reconstruction.

Afghanistan's problems were never going to be solved in a year, but the euphoria which comes with the end of a war generates unrealistic expectations. After 23 years of praying for safety and jobs, Afghans may, understandably, find it hard to have to wait any longer.

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Japan

Frozen politics

Dec 5th 2002 | TOKYO
From The Economist print edition

The opposition leader bows out

YUKIO HATOYAMA, the leader of the Democrats, Japan's main opposition party, announced his resignation on December 3rd. He will officially step down in mid-December, at the end of the current session of the Diet, the parliament. The Democrats are already squabbling over who should replace him, and their supporters hope that the change will somehow stir the party from its torpor.

Mr Hatoyama, the grandson of a former prime minister, left the ruling Liberal Democratic Party (LDP) in 1993 and eventually helped to form the Democrats in 1996, bringing in other parties two years later. Recently, he surprised fellow Democrats with a bid to merge the party with the Liberal Party, led by Ichiro Ozawa, a former LDP heavyweight. But he has never managed to unite the Democrats' fractious groups.

The party has been an uninspired and often inconsistent opposition to the LDP. This prompted several candidates to run, unsuccessfully, against Mr Hatoyama in September's party elections. The cries for his resignation grew louder after the Democrats' terrible showing in October's by-elections, in which they won only one of seven contests.

The Democrats have called a meeting for December 10th to select Mr Hatoyama's replacement. Naoto Kan, the previous secretary-general, finished second to Mr Hatoyama in September, and is now the front-runner. Mr Kan's many detractors, however, say that he achieved little as secretary-general, and are pressing for another choice.

None of this seems likely to fix what really ails the Democrats. Even if the party goes on trying to merge itself with other groups, it is dealing mostly with fellow pipsqueaks. The Democrats have only 5% support in opinion surveys; the Liberals only 1%. Many of the LDP's detractors have expressed hopes that young opposition leaders would join forces with their young counterparts in the ruling party in a bid to revive Japanese politics. That would be a welcome move; but it hardly seems imminent.

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Security after Bali

The elusive tourists and their dollars

Dec 5th 2002 | JAKARTA
From The Economist print edition

Australia promises to strike at terrorists in other countries

A REASSURING sight in Jakarta these days is security guards with metal detectors checking cars parked outside office blocks. True, in one such operation no cars were checked after 9.30 in the morning. Presumably, terrorists are thought to be early risers. Nevertheless, by Indonesian standards, the overall improvement in security since the Bali bombings of October 12th has been impressive. Even after a series of deadly terrorist attacks in Jakarta in 2000, ordinary people were offered little protection. Only the rich and powerful were made to feel secure. The Bali bombs, and the prospect of losing millions of tourist dollars, have made a difference. If the bombers wanted to inflict further damage on Indonesia's weak economy, they succeeded.

A Bali-type bombing seems depressingly easy to repeat. Clive Williams, head of terrorism studies at the Australian National University, believes the Bali attack was essentially a home-grown affair, comparable with attacks on western tourists in Egypt. The bombers may or may not have had money from al-Qaeda. Most Muslim militant groups around the world have probably had support from al-Qaeda at some time, he says. But, for all its bloodiness—it claimed some 190 lives—the Bali attack probably cost little money.

The hopeful news is that the Indonesian police force has been more successful than many people expected. The country's rare decision to allow foreign policemen to help with the investigation has given it access to sophisticated forensic tools. An Indonesian called Mukhlas, said by police to have masterminded the Bali bombing, was detained on December 3rd. Two others are held in connection with the bombing, Imam Samudra and his accomplice, Amrozi. Mr Samudra has fought in Afghanistan.

In the search for other possible bombers there is talk of re-opening investigations into a number of bombings of churches in Indonesia on Christmas eve, 2000. Those in custody in connection with the church bombings may be questioned again, along with others who were never charged. There are also suggestions of a connection with Malaysia; a group suspected of terrorism, Jemaah Islamiah, operates in that country.

The Australian prime minister, John Howard, upset Indonesians and others this week with a threat to strike against militants outside Australia if they are believed to be planning an attack on his country. Australian diplomats in the region tried to soften the impact of Mr Howard's remarks by saying, implausibly, that he wasn't referring to the region. But Indonesia, Malaysia, Thailand and the Philippines all took offence. The Malaysian prime minister, Mahathir Mohamad, said that this was not the way to tackle terrorism. Nor is it a guaranteed way to lure tourists to what not very long ago were thought of as the peaceful tropics. People in Australia, on the other hand, may feel that it is better than waiting to be hit first.

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The pressure on Iraq

Inspecting, squeezing, threatening

Dec 5th 2002 | CAIRO
From The Economist print edition

AP

With Iraq half-bending under the strong-arm tactics of America and the United Nations, the Arab world holds its collective breath for the next stage

Get article background

AS THE fasting month of Ramadan ends, and the December 8th deadline for Iraq to disclose its weapons programmes nears, anxiety is mounting in the Arab world. Western pressure on Saddam Hussein's regime, both physical and verbal, continues unabated. Those who are applying the squeeze see Mr Hussein's wary co-operation with the Security Council as a vindication of strong-arm tactics. The Islamic faithful see Mr Hussein as a victim of American bullying.

The UN weapons inspectors have been niggled at by the Iraqis for spying and by the Americans for being too soft. But on the whole the inspections have gone well, so far. Before the programme was suspended in 1998, Iraq had denied the inspectors access to some sites on grounds of “national honour”. Yet this week guards opened the gates to a presidential palace compound in central Baghdad with hardly a murmur. Inspectors visited a dozen other sites unimpeded, but have yet to exercise further intrusive privileges, such as the right to use drones and helicopters, and the right to take Iraqi technicians outside the country for interview.

The more immediate test comes with Iraq's disclosure list. In another show of accommodation, Iraqi officials declared that they would produce the declaration a day early. The list, they said, would describe their biological, chemical, missile and nuclear technologies, but would also, they insisted, confirm Iraq's contention that it has nothing to hide.

Much hinges on this declaration. The Security Council's Resolution 1441 says that omissions or “false statements” would constitute a material breach of its rules, and therefore represent grounds for the use of force. Donald Rumsfeld, the American secretary of defence, said this week that “any country on this earth with an active intelligence programme knows that Iraq has weapons of mass destruction.” He added that if Iraq's declaration fails to satisfy, America would not necessarily wait for UN approval to strike Baghdad. His deputy, Paul Wolfowitz, trimmed this message a little when he told NATO ambassadors on Wednesday that Iraq's declaration would not, in itself, trigger a decision on military action.

Yet the threat is there and, backing it up, America is pursuing a military build-up that has doubled its

manpower in the region since September to some 50,000, including at least 10,000 troops in Kuwait. Recent naval redeployments suggest that up to five of America's 12 aircraft carriers may be stationed around the Gulf by mid-December. Exercises to test a newly-installed American command-and-control facility in Qatar are to be held next week, with Mr Rumsfeld in attendance.

British and American aircraft, meanwhile, continued their heightened patrolling, and bombing, of the so-called no-fly zones that cover two-thirds of Iraq's territory. Since September they have dropped over 1m leaflets warning Iraqi forces not to provoke them; they have also struck 20 separate targets on 13 occasions since Iraq declared its co-operation with Resolution 1441 in early November. This has prompted successive Iraqi complaints to Kofi Annan, the UN's secretary-general.

The muscle-flexing has been matched by shows of diplomatic force. As the British government released a report designed to remind the world of the Iraqi regime's past atrocities, it also pointedly invited Bashar Assad, until recently thought to be an Iraqi sympathiser, for the first-ever state visit by a Syrian president. The atrocities committed by Mr Assad's father are now, presumably, to be forgotten.

Bargains with the neighbours

Mr Wolfowitz flew to Turkey, a geographically crucial staging post, to bargain for a bigger Turkish contribution to any future war effort. America's determination to enlist the Turks was underscored by promises of both financial aid and all-out support for Turkey's long-sought admission to the European Union. In return the Turks said that they would allow American troops to use their air space and facilities, but only if there was a second UN resolution endorsing military action.

Iran, another powerful neighbour, hinted that it would enhance co-operation with the country it used to call the Great Satan. It might provide its own intelligence on Iraqi weapons development, and might also give a green light for the Tehran-based Iraqi opposition to collaborate with any American plan for “regime change”.

Iraq's third big neighbour, Saudi Arabia, was meanwhile put on the defensive by a barrage of accusations in Washington that it is soft on terrorism. Extricating itself from the charges may involve, as a quid pro quo, a stronger show of support for American policy towards Iraq.

Quiet American diplomacy in Arab capitals also seems to be producing the desired result. This does not necessarily mean overt action to squeeze Iraq, which would be difficult given the Arab public's strong and undiminished hostility to American policy. Simple inaction may turn out to be good enough. For example, calls by Arab commentators for a concerted offensive to stave off an American attack on Iraq have been met by a stony silence from Arab leaders.

The only real comfort Mr Hussein is getting comes, oddly enough for a secularist whose regime has assassinated prominent clerics, from mosque pulpits. In a sermon delivered on November 29th before an estimated 2m pilgrims gathered for the final Friday prayers of Ramadan, the imam of the Great Mosque at Mecca called on God to spare Muslims from “the evil of tyranny”, by which he was assumed to mean the United States. And an on-line *fatwa*, on an Islamic website that is considered to be both moderate and mainstream, instructed believers that to co-operate with America in attacking Iraq would be “a grave crime and a heinous sin”.

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Jordan and its Palestinians

The queen outmatched

Dec 5th 2002 | AMMAN
From The Economist print edition

Her demographic coup blown away by Jordan's indigenous tribes

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AP

Rania with her countrymen at heart

SHOULD Jordanian women have equal rights with men to pass on their citizenship? Yes, ruled Jordan's government this week—unless they happen to be Palestinian. In the battle to keep their supremacy, Jordan's indigenous minority of East Bankers have launched a successful counter-attack against last month's decree by Rania, their Palestinian-born queen, that mothers as well as fathers can pass their nationality on to their children.

Newspapers run by East Bankers accused the queen of using the cover of sex equality to naturalise hundreds of thousands of her Palestinian kinsmen in Jordan, and convert their homeland into Hashemite Palestine. If we do not stop the queen, they cried, we will be swamped. The Jordanian cabinet, bruised from last month's gun-battles with East Bankers in Maan, listened and backed down. No new rights to citizenship had been granted, they said. Applications for nationality would be treated on a case-by-case basis. Palestinians accused cabinet members, most of whom are East Bankers, of plotting to keep them second-class citizens.

No Arab state has done more for the Palestinians than Jordan. The kingdom plays host to one of the world's largest concentrations of refugees, and has given them more freedom and passports than any other country. Last summer, Jordan for the first time admitted that 43% of its 5.3m citizens were of Palestinian origin. But hundreds of thousands more are estimated to reside in the kingdom on temporary passports, with no right to vote, or get free treatment in government hospitals.

Before the cabinet chipped away at the queen's decree, columnists had predicted that a wave of up to 250,000 Palestinians would gain citizenship. Thousands more would flood in as Palestinian girls with Jordanian passports married their cousins over the river to spare them the miseries of Israeli military rule.

In an attempt to soothe tempers, King Abdullah has carpeted his kingdom with billboards emblazoned with the slogan “Jordan First”. Special courses are to be taught in schools inculcating a new national identity. People, or so he hopes, are to be merged into a single stock, in which their origins, whether Palestinian or tribal Bedouin, would no longer count.

The East Bankers are deeply distrustful. Some 80 years ago, they invited the king's great-grandfather to set up in their homeland, and for generations they have reaped the benefits. Today they ask how long the old rules will apply. A privatisation programme has boosted the fortunes of the Palestinian financiers who dominate the private sector. It has hit the poorer East Bankers, who have lost their jobs in failing state enterprises. Many have also lost their privileges: nowadays if a tribal big shot reneges on his water bill, his supply is cut. If all the Palestinian-born were granted nationality, their land, they fear, would no longer belong to the Bedouin.

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Israeli politics

A dull and fuzzy campaign

Dec 5th 2002 | JERUSALEM
From The Economist print edition

The bipartisanship of a nation at war

Get article background

AP

Happy, Teflon-plated Sharon

BUOYED by his triumph over Binyamin Netanyahu in the Likud party primary, Ariel Sharon made a first, gentle stab at electioneering this week. “Our rivals”, he told a party rally on December 2nd, were supported by “our enemies”. In other words, the Palestinians would prefer it if Labour, now led by the doveish Amram Mitzna, defeated the Likud in the general election on January 28th. Mr Mitzna, he added sneeringly, had sought “letters of recommendation” from Arab leaders: a reference to a polite correspondence between Labour's new leader and Egypt's president.

Mr Mitzna for his part asserted that the prime minister was “the same Sharon as in 1982”, when he, a young brigadier, offered to resign his commission rather than continue serving in the reckless invasion of Lebanon instigated by Mr Sharon, who was then defence minister.This failed to ruffle the determinedly courteous and grandfatherly Mr Sharon. The Likud's lead is so wide—41 seats in the 120-seat Knesset against Labour's 20 in one recent poll—that much of the drama seems to have fizzled out of the campaign. Many people believe that not only is the result a foregone conclusion, but that the resuscitation of the still-warm Likud-Labour unity coalition after the election is pretty much a done deal. Mr Sharon keeps saying that he wants it, and Mr Mitzna, significantly, has stopped saying that he doesn't.

The flat campaign and the yen for unity reflect a blurring of formerly firm lines of dispute. Mr Mitzna's plan to withdraw unilaterally from Gaza within a year appeals to more than half of the public. And more than half of Likud voters say they accept a Palestinian state. Mr Sharon himself spelt out his proposals for a “state” this week. But his concept of a fragmentary and unviable entity, covering about 40% of the West Bank and 70% of Gaza, is a far cry from what Mr Mitzna envisages.

There is obfuscation afoot, some of it deliberate. When the ambassador to the UN voiced Israel's acceptance of two states living side by side, Mr Sharon's aides slapped him down. And the army chief of staff was quick to deny this week that he had told a Washington think-tank that most Israelis assume that most settlements will eventually be dismantled.

But it is not all double-talk. New realism among Likud supporters transcends semantics. And, on the left, there is broad support for harsh military measures against the Palestinians. The two *intifada* years have developed the dulled and fuzzy politics of a nation at war.

He has done his best, they say

How otherwise to explain Mr Sharon's remarkably high rating? People tell pollsters of their constant fear of terror, of their sharply worsened economic condition. They freely acknowledge that Mr Sharon has not provided the “peace and security” he promised two years ago. And yet, so many say, he is doing his best in a dire situation not of his own making.

Attacks like the two in Mombasa on November 28th feed this atmosphere of bipartisan togetherness. The one that partially succeeded, a suicide car-bombing of an Israeli-owned hotel, killed three Israeli tourists

and ten Kenyans. But the one that failed—two shoulder-fired Strella missiles that just missed a full Israeli charter plane taking off from Mombasa—brought Israel face to face with mega-terror.

Al-Qaeda, in an Internet message, claimed credit this week for the terrorism. Ephraim Halevy, Israel's national security adviser and until recently head of Mossad, Israel's secret service, gave warning on December 2nd that were an act of this magnitude to succeed, it would change Israel's policy and behaviour cataclysmically.

Mr Sharon's own behaviour changed briefly during November 28th, which was also the day of the Likud's primary election. As the day waned, he panicked, realising that the shock of Mombasa, and also a Palestinian attack that afternoon on the Likud office in a northern Israeli town, were keeping the party faithful at home. His commanding lead over Mr Netanyahu threatened to shrivel. “Go out and vote, go out and vote,” he bawled into the cameras at a hastily held press conference. In the event, just under half the Likud's 310,000 members voted, and Mr Sharon won by a comfortable 15%. Pundits waxed furious at his abuse of his office for party-political purposes. But the old warrior's Teflon-plated armour remains unmarked.

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Congo's bewitched children

Sad little sorcerers

Dec 5th 2002 | KINSHASA
From The Economist print edition

Many of Congo's street children are fleeing accusations of witchcraft

Get article background

STREET life in Kinshasa, Congo's capital, is uncomfortable. The air is foul and humid, like being licked by a pack of stray dogs. The squalor can be unnerving: a human foetus was found in the trash last time the central market was properly cleaned. The city is so poor, and its government so corrupt, that even the man who fills in the same pothole each day on Lukusa Avenue, in exchange for tips from motorists, is regularly shaken down for bribes by the police. But perhaps Kinshasa's saddest sight is its army of under-age “witches”.

They call them witches

By one estimate, there are 40,000 street children in Kinshasa, of whom 80% have been kicked out of their homes because their families thought they were witches. Such figures are, like most Congolese statistics, unreliable. But the problem is undoubtedly real. It is also relatively new. The Congolese used to blame their leaders for their horrific problems, but many now blame juvenile necromancy instead.

With broods of ten commonplace, there are plenty of children to accuse. Death or disease in the family is often taken as evidence of sorcery. Failed crops, lost jobs and bad dreams also arouse suspicion. Midway through last year, several hundred children were turfed on to the streets of Mbuji-Mayi, a mining town, after a sudden drop in diamond prices sparked fears that tiny hands were casting spells.

Even relatively affluent Congolese seem convinced of the evil powers of bewitched children. But the children themselves plead innocent: they know what crimes they have been accused of but not why. Olivier, for example, a grubby nine-year-old with a blue plastic crucifix bobbling against his belly, says he was accused of killing his mother with AIDS after he prayed by her death-bed. Ibrahim and his brother Yves, aged ten and seven, say they were fingered for the same crime, but several months after the event. They were sent to an aunt, who hardly fed them, and then took their skinniness as proof that they were witches.

Belief in witchcraft is widespread in Africa. But the habit of blaming children is at odds with one of the most enduring and attractive features of Congolese culture: the extended family. Surplus children have traditionally been farmed out to wealthier relatives and friends.

But as Congo has grown poorer, the system has come under strain. Alain and Ordey, pint-sized, urchin brothers, spent their earliest years in their grandfather's compound, surrounded by uncles, aunts and a crowd of cousins. Then, their grandfather fell ill and his business failed, five of their uncles died, and their mother became a prostitute and disappeared. Finally, the boys' grandfather pinpointed the culprits—and cast the boys out to beg and steal on Kinshasa's streets.

Congo's rulers are too concerned with their own survival to spare a thought for the country's homeless child sorcerers, but aid agencies in Kinshasa are now debating what to do about them. Not all aid workers treat the problem as a purely social one, however. A Congolese programme officer at one American agency says, “The biggest problem is knowing how to sort the real witches from the rest.”

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The European Union

Eastward ho!

Dec 5th 2002 | BRUSSELS
From The Economist print edition

Ten would-be members can expect a welcome from the EU at a summit in Copenhagen next week. But what about Turkey?

Get article background

“THIS is a great moment,” insists Marek Grela, Poland's ambassador to the European Union. “It marks the final burial of the totalitarian era of the last century and a final end to the division of Europe.” The ambassador's insistence on the historic nature of the decisions the European Union will make at its summit in Copenhagen on December 12th and 13th is appropriate—but also slightly plaintive. It has taken almost five years of tortuous negotiations to get to the point where the EU's 15 current members are at last almost ready to strike a deal to admit ten new ones: Poland, Hungary, the Czech Republic, Slovakia, Slovenia, Lithuania, Latvia, Estonia, Cyprus and Malta. But the widespread assumption that the deal is all but signed has drained away much of the sense of occasion that would otherwise have attended the negotiations' final stages. Attention is already straying towards a country whose membership of the EU is still far from assured: Turkey.

The fact that a deal on EU enlargement is now so close is a tribute to both the determination of the candidate countries and the grinding efficiency of the EU's negotiating machinery. As little as two years ago, it seemed implausible that as many as ten countries would really sign a deal at the end of 2002, allowing them to join the club in May 2004. To get to this stage, both sides have had to cut their way through a thicket of thorny issues, from the free movement of labour and capital to the enforcement of environmental rules and the regulation of state aid to industry.

The small print

In theory, the candidates are meant to implement all 80,000-plus pages of EU law immediately; and the EU is meant to grant the candidates all the rights of membership just as quickly. In practice, political and economic constraints on both sides mean that in a host of areas transitional deals have had to be struck. The EU's current members have insisted on an interim of seven years before there is fully free movement of labour, and ten years before the new members are eligible for the full range of farm subsidies. For their part, the candidates have been granted extra time to phase in the EU's burdensome environmental legislation. Each country has sought a range of concessions tailored to local sensitivities, from the Estonians' wish to continue shooting bears to Malta's insistence on banning the purchase of second homes by foreigners.

A week before the summit, there were still issues to be settled. The hardest concerned money and agriculture, subjects closely related in the EU, which still spends over 40% of its budget subsidising farmers. All the candidate countries were still insisting that the EU's offer on phasing in subsidies to farmers was not generous enough. An attempt by the Danes, who are chairing the final stage of negotiations, to offer a more generous settlement had been knocked back by the Germans, the Union's traditional paymasters, who are under growing financial pressure at home.

Among the candidates, Poland is fighting hard to get an increase in its quota for milk production, arguing

that its farmers will be bankrupted if the quota is set too low. And there are still small but delicate local concerns. The Latvians, for instance, got a last-minute dispensation to catch under-size herring, a local speciality; the Czechs are still fighting hard over the geographical designation of Budweiser beer.

Everybody agrees that it would be unseemly if the great “reunification of Europe” were to be overshadowed by ungracious last-minute haggling over money, let alone herring and beer. But it is now clear that some such delicacies, large and small, will indeed end up on the plates of the prime ministers and presidents assembled in Copenhagen next week. One Central European diplomat comments: “We'll need a little bit of drama—just to make sure that people are paying attention.”

Last-minute dramas can get out of hand. But it is hard to believe that the summit will end without a victory photograph of the new and enlarged EU family. On the edges of the picture will be Romania and Bulgaria, two would-be members which have yet to complete negotiations but which are hoping to join the club in 2007. However, one big question will be overshadowing the summit: Turkey.

The Turks were first offered the prospect of eventual membership of the European club in the early 1960s, when the Central Europeans were still locked behind the iron curtain. The EU has procrastinated and hummed and hawed. Every now and then eminent European politicians have decried the very idea of Turkish membership, the latest being Valéry Giscard d'Estaing, a former French president now chairing a convention on the EU's future. But the Turks have kept pressing for a date to start negotiations and their pleas are increasingly difficult to ignore.

The sight of ten more countries about to join the EU naturally puts Turkish claims higher up the agenda. And the United States, which, for its own strategic reasons, badly wants Turkey admitted to the EU, is fiercely pressing the Europeans to let it in. The Turks themselves have pushed through a clutch of legal and political reforms, for example abolishing the death penalty and easing restrictions on the Kurdish minority, which have gone a long way towards meeting the EU's “Copenhagen criteria” of minimal democratic norms that all countries must meet before they can begin negotiations to join.

So what will the summit offer the Turks? Three possibilities are being discussed: “a date”, “a date for a date” and “a rendezvous”. The Turks want a straightforward date: a definite moment for starting negotiations. But they know that they are unlikely to get that, so their fall-back is a date for a date: the promise that if certain specified reforms are in place by a given moment—say, the end of 2004—negotiations will then begin. The Europeans are still toying with the idea of offering a vaguer commitment: a rendezvous at which both sides would meet again to assess progress at a later date. The Turks dismiss this last option as meaningless.

Quite what offer Turkey will get may not emerge before the summit. If the Turks accept the UN's peace plan for the divided island of Cyprus by the time of the summit, their case may be irresistible. But even without a breakthrough over Cyprus, things seem to be moving Turkey's way. Even Mr Giscard d'Estaing's recent intervention may have worked to its advantage, by forcing European leaders to restate support for eventual Turkish membership.

Certainly the Turks themselves are sounding smoothly confident. “Giscard's statements are understandable,” says a top Turk. “He's of a certain generation still nostalgic for a small, homogeneous EU. But that Europe has gone for ever.”

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About sponsorship

France, Germany and the EU

The old motor revs up again

Dec 5th 2002 | BERLIN AND PARIS
From The Economist print edition

France and Germany are trying to get back into the EU's driving seat

Get article background

AP

Natürlich, Jacques. Evidemment, Gerhard

IT ISN'T yet back to full throttle. But, suddenly, the Franco-German motor that used to power the European Union is revving up again, as a series of joint initiatives has lately shown. And Britain, whose diplomats briefly tried to make out that the initiative had passed to Tony Blair, is yet again in the back seat.

Jacques Chirac and Gerhard Schröder are not as close as some of their predecessors. Even before Mr Schröder was elected chancellor in 1998, he had irritated the French president by urging that the Franco-German duo become a trio, taking in Britain. At the EU's Nice summit in 2000, the pair fell out fiercely when Mr Chirac, rebutting a German claim for greater voting weight in the Council of Ministers, offensively recalled the three German invasions of France between 1870 and 1940. And in the recent German election Mr Chirac ostentatiously backed Edmund Stoiber, Mr Schröder's conservative challenger.

Even now, the two men have different views of the EU's expansion, which France sees as strengthening German influence, though, dining together on December 4th, they did promise a joint position on Turkey and other enlargement issues at the coming EU summit. They differ about the Union's future shape, Germany being more federally minded, France more careful of national sovereignty (though this week it made some gestures Germany's way). They differ on farm policy, Germany being the big payer, France the big recipient, of EU bounty.

Yet the two reckon that if they do not work together the EU will stick in the mud. Hence the words of Mr Chirac's foreign minister, Dominique de Villepin, in Marseilles this week: yes, they have differences, but what counts is “our determination to overcome these... in the service of the European enterprise”—and, he could have added, of France's influence therein.

The joint initiatives have come thick and fast. In a brief meeting before the EU's Brussels summit in October, Mr Chirac and Mr Schröder, to British fury, agreed on farm spending: a ceiling, to calm the Germans, fearful of the future members' demands, but no radical or early reform, to keep France's farmers sweet and so to avoid any French obstruction to enlargement. Soon came a joint paper calling for flexibility in the EU's notorious stability pact. Here there was a common interest: Germany is probably over the pact's budget-deficit limit—3% of GDP—already; France risks heading that way.

Then came a joint paper to the EU's constitutional convention on defence issues. It suggested more co-operation (to be decided by majority vote), the creation of multinational forces with “integrated command capability”, harmonisation of weapons planning and a European armaments agency. This was more striking, though likely to stay hot air. In terms of hardware, training and readiness, military or political, for action outside Europe, “European” defence has till now been a Franco-British affair, sealed at a bilateral summit at St Malo in 1998 and symbolised by talk of an EU rapid-reaction force to which the two would be the big contributors. Germany is cutting defence spending.

Last week brought a joint Franco-German paper on justice and home affairs. It suggested an EU prosecutor's office, shared policies on migration, cross-border police investigations, and, not least, majority voting on such matters. Soon to come is a paper on economic governance and tax

harmonisation—a notion that rings still more alarm-bells, in London and elsewhere. More ideas will no doubt follow, as the two countries celebrate, on January 22nd, the 40th anniversary of the bilateral treaty that sealed their post-war reconciliation.

Though they exchange *tu* and *du*, Mr Chirac and Mr Schröder do not much like each other; indeed, for all the Blair-Chirac spat in Brussels, both get on better with Mr Blair (who, via *Paris Match*, an illustrated weekly, has just sent the French president a vast verbal let's-make-it-up bouquet of roses). But Britain, for all Mr Blair's less-than-secret longings, is outside the euro-zone; firmly for a firmly intergovernmental EU; and closer than other EU countries to American policy, especially on Iraq.

De Gaulle once famously said that, forced to choose between Europe and the wide world, Britain would always choose *le grand large*. Even now, after it has been nearly 30 years inside the EU, many continentals agree with Joschka Fischer, Germany's foreign minister, speaking in 1998: “Britain just doesn't know what it wants.”

In contrast, with the uncertainties of French “cohabitation” between a right-wing president and a left-wing prime minister over, and with both leaders due for a good few years in office, now is plainly the time to try cranking up that Franco-German motor again. Whether the conditions will ever be right again for the smooth ride of old is still, however, open to question.

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Turkey's secularism

The dreaded headscarf

Dec 5th 2002 | ANKARA
From The Economist print edition

The generals find fault

Get article background

EPA

Scarved fundamentalists?

THE generals are sticklers for protocol. So when Bulent Arinc, the Turkish parliament's new speaker, from the ruling Justice and Development Party (AK), took office late last month, the chief of the general staff, General Hilmi Ozkok, flanked by his top commanders, paid him the traditional courtesy call. It lasted just three minutes.

The generals are the fundamentalists of Turkish secularism, and they are suspicious of AK, which has Islamic roots. But what exactly had the new speaker done to offend them? When he went to Ankara's Esenboga airport to see off President Ahmet Necdet Sezer and his spouse Semra as they departed for Germany on a state visit, he took his wife with him. No problem. The problem was with Mrs Arinc's head: in keeping with Islamic tradition, she puts a scarf on it. Her scarved presence on an official occasion, say the pro-secular purists, was a deliberate AK provocation.

By those standards, two-thirds of the 25 AK ministers, including the prime minister, Abdullah Gul, will need to keep their spouses out of the public eye. Emine, the wife of Recep Tayyip Erdogan, the AK chairman, is another scarf-wearer. So are their two daughters, who are now studying in the United States, because the scarf is banned at Turkish universities. Mr Gul's daughter, a student at Ankara's Bilkent University, is said to take off her scarf to go to classes. Other observant young women there evade the ban by wearing wigs.

The headscarf debate symbolises the tensions between openly pious Turks and a vocal (and mainly elite) minority to whom the “turban”, as they call it, is a symbol of Islamic fundamentalism which, they say, threatens not only Turkey's secularism but its European aspirations too. It was that sort of thinking that propelled Kemal Ataturk to urge Turkey's women to cast off their veils more than 70 years ago. Yet more than half still cover their heads, in one way or another. In much of rural Anatolia they do so out of tradition. But for millions of migrants to big cities like Istanbul or Izmir, the headscarf is a symbol of their identity.

“As long as these women remained out of sight, on factory floors, it was OK,” says Jenny White, an American anthropologist who spent seven years in Istanbul's working-class Umraniye district studying the roots of political Islam. But as the new generation began to attend universities it clashed with the secularists. The scarf “became a class issue. It has very little to do with Islam,” says Ms White.

Maybe. But the generals and the no less secularist judiciary remain unswayed. The pro-Islamic Welfare Party was banned in 1998, as was its successor, Virtue, in 2001, in part because of their efforts to end the ban on the headscarf in government offices, parliament and universities. President Sezer backs this secularist view. As a constitutional-court judge, he once overruled a government decree that would have allowed headscarves on campus.

Mr Erdogan, who insists that his party, whatever its roots or its members' beliefs, does not have an Islamic agenda, appears to have got the message. “The headscarf issue”, he declared last week, “is not among our government's priorities.”

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Sweden and the euro

Persson goes for a referendum

Dec 5th 2002 | STOCKHOLM
From The Economist print edition

Selling the euro idea to Sweden's voters will take some doing

Get article background

FRESH from re-election in September's general election, Sweden's prime minister, Goran Persson, has a new goal: to persuade Swedes to abandon their national currency, the krona, in favour of the euro.

Last week, in agreement with the leaders of the other parliamentary parties, Mr Persson set a date for a referendum on the issue, September 14th next year. The leaders will meet again later this month to determine—jointly, a lesson for some less democratic countries—the wording of the question, and how the rival campaigns are to be funded.

To get a firm date was another victory for Mr Persson, who only recently managed to persuade his Social Democratic Party that its economic preconditions for adopting the euro had been meet. These are that Sweden's economy be in sync with that of euro-zone countries, wages moving stably, and public finances healthy enough to allow manoeuvre in case of an economic slowdown.

Voters, however, are unenthusiastic. Polls now show the yeses and the noes running neck and neck; indeed one survey has put the noes in front, for the first time in 18 months. The Greens and the formerly communist Left Party, who usually help Mr Persson in parliament, are strongly against, and even his own followers are less keen than he is. Some ministers have openly expressed doubts, and one of his members of parliament claims that Social Democratic voters will mostly say no.

The fear on the left is that Sweden will be forced to abandon not just its currency but its cherished welfare state. And, with no independent monetary policy, the only way to lessen wage pressures will be higher unemployment, the left argues. This worries LO, the powerful blue-collar trade-union confederation. It wants a huge buffer fund set up, for use in a downturn.

Backed by business and the main political parties, and offering dreams of lower prices and interest rates, the euro's prospects still look fair. But in Denmark, as Sweden's political elite well remembers, a pro-euro majority evaporated during a bitter referendum campaign in 2000. Events beyond Mr Persson's control could derail his plans. Swedes have a rich vein of scepticism about the EU. And selling the alleged economic benefits of the euro may not be easy: Sweden now has higher growth, less unemployment and stronger public finances than the euro-zone.

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Italy's budget

Rose-tinted economics

Dec 5th 2002 | ROME
From The Economist print edition

Italy's 2003 budget hotchpotch has upset almost everyone

BOUNDLESS optimism is among the most obvious, and to many Italians one of the most attractive, of the traits of Silvio Berlusconi, their prime minister. He can look nasty facts straight in the face and deny them. But the 2003 budget, now on its way through the legislature, is sorely testing his ability to keep smiling.

Prime minister since mid-2001, he has always taken a rosy view of the economy. His government started by looking forward to growth of 3% a year. But the downturn had already begun. A few months ago, the government still said it expected more than 2% this year. Now it says 0.6%.

Modest enough? No. Confindustria, the bosses' club, says 0.4%. Well, insists the government, things will perk up next year. Its budget calculations now depend on growth of 2.3%. No, says Confindustria: under 2%. The European Union puts growth at 1.8%, and predicts a budget deficit of 2.2% of GDP, against the government's 1.5%. Mr Berlusconi is crossing his fingers for upturns in the American and German economies—and for peace in Iraq.

If his figures do have to be revised, Italians can expect corrective measures in the first half of next year. But what stomach will Mr Berlusconi and Giulio Tremonti, the minister for economic affairs, have for raising taxes and cutting spending next spring or summer? They found it hard enough getting this budget through the lower house of parliament. The tax-and-savings package, worth *euro*20 billion ($20 billion), has left many Italians dissatisfied.

The budget has reunited Italy's three trade-union groups, craftily split by the government earlier this year. Worse for Mr Berlusconi, it has turned Confindustria, once an ally, into an opponent. Up and down Italy, mayors and regional authorities of all parties are squealing: they will bear most of the *euro*8 billion of cuts. Reductions in cash for universities and research caused a row between Mr Tremonti and Letizia Moratti, the education minister. The poor south is to get nothing extra, while the Northern League, a fractious member of the government, has twisted Mr Tremonti's arm for more for supposedly poor northern districts.

Mr Berlusconi has had to defend Mr Tremonti, a tax expert who seems happier ordering amnesties enabling people to bring back money illegally salted away abroad than assessing business cycles. Although the public-sector accounts of Germany and France are now the EU's main concern, Italy's are basically more worrying. At almost 110% of GDP last year, its public debt is relatively much bigger than Germany's or France's.

In sum, the government's economic record looks shaky, and its ability to obey Europe's rules is suspect. Its priority has not been the economy, says Enrico Letta, the centre-left opposition's economics spokesman, but legislation on the criminal code (that is, in ways helpful to Mr Berlusconi and some of his friends). Meanwhile, he has yet to tackle such vexed issues as pensions. The budget in essence prescribes once-off measures to plug holes.

Retreating from free-market economics, Mr Berlusconi's team is making noises about lifelines for troubled private-sector firms. The public sector may be asked to find money to save a factory in Sicily owned by Fiat. Mr Berlusconi's coalition won a clean sweep of the island's 61 seats last year and these MPs are threatening to boycott the budget. The agriculture minister wants to bail out a tomato-canning firm. Mr Berlusconi's business skills have not done much for Italy's economy.

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The Prestige oil spill

Spreading

Dec 5th 2002
From The Economist print edition

Spaniards quarrel, frigates sail and the EU does its best to slam the stable door

AP

There's more where that came from

IT BEGAN with a worn-out tanker; became a series of gigantic oil slicks as the *Prestige* tore apart, and ultimately sank, off north-west Spain; then, as the heavy fuel oil slurped ever more widely ashore, it brought disaster to that region's many fishermen. By this week it had become a flaming political row in Spain, and one of the rare events to prod the European Union into almost instant reaction.

The Spanish row was mainly cat-calls, though it could have electoral effects. The media had rapidly discovered that Manuel Fraga, premier of Galicia, the region where the oil came to shore, had gone off on a shooting holiday—accompanied by the region's environment minister, no less—some days after the trouble began. But the real fury was soon aimed at the central government, accused not just of early decisions that had spread the pollution much more widely than need be, but of having neither the will nor the equipment to prevent the oil reaching land, nor—the real complaint—to clean up when it did. While foreign ships sucked up the oil at sea, and even some Belgian troops helped clear it from the beaches, last Sunday a crowd put at 150,000 marched through Santiago de Compostela, Galicia's capital, calling for Spanish political heads to roll.

The government—like Galicia's, run by the People's Party—hit back with abuse, denouncing its Socialist critics as “carrion-scavengers” trying to make party points out of a national disaster. One minister even hurled at them the “dirty war” waged against Basque terrorists by a Socialist government in the 1980s. You don't understand democracy, bawled back the Socialists, the Galician “nationalists” and their media allies. King Juan Carlos went to see the oil-covered beaches and the filthy clear-up for himself; the prime minister, Jose Maria Aznar, wisely didn't.

The oil's effects went wide. As it spread down Spain's western coast and along the north, Portugal raised the alarm, and France did likewise for its own south-west around Biarritz. The Spanish and Portuguese navies ordered a Russian tanker out of their waters. France sent a frigate to make sure one ancient vessel much like the *Prestige* stayed out of its. A similar antique, chartered by the same Russian oil company that had chartered the *Prestige*, was told not to enter the English Channel.

In Brussels, the European Commission rushed out proposals to ban vessels built and laden like the *Prestige*—single-hulled and carrying heavy oil—from EU waters, within the next couple of months. It published a list of more than 60 ships that it considered suspect in themselves, and proposed penalties for negligence at sea. Suddenly, if more in theory than reality, a maritime-safety agency that has long been on the EU stocks was formally launched, as EU transport ministers met this week.

There was just one snag, a familiar one: the ministers agreed to launch the agency, but were expected to drift, if not to run aground, with the other proposals. The European Commission proposes, but national interests have the last word.

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Charlemagne

The Brussels consensus

Dec 5th 2002
From The Economist print edition

Why subversive thoughts are frowned upon in the would-be capital of Europe

EARLIER this year, Robert Kagan, an American historian, suddenly became a celebrity in Brussels, after he wrote an article for *Policy Review*, an American journal, arguing that Europeans and Americans have fundamentally different attitudes to the world. Americans, he declared, were “Hobbesians”, at ease with the use of force; Europeans were “Kantians”, yearning for a world of perpetual peace in which all difficulties are settled by multilateral discussion. The article hit a nerve. Javier Solana, the European Union's foreign-policy chief, suggested that all his staff should read it. Chris Patten, his counterpart at the European Commission, wrote articles challenging the “Kagan thesis”. Mr Kagan himself was invited to innumerable seminars.

An arresting article appearing at the right time is always liable to create a stir. But the Kagan thesis also made waves in Brussels for another reason. It was an example of the kind of iconoclastic analysis which, while quite common in Washington, is still very rare in Europe's self-styled capital. American think-tanks revel in sharp ideological conflict and their occupants strive, sometimes too hard, to come up with the next “big idea”. Intellectual life in Brussels is different. An American academic familiar with its think-tanks calls the atmosphere “almost Soviet. It is as if they are afraid to work on something, unless the commission has decided that it should be on the agenda.”

This may seem odd. After all the EU is going through a profound political transformation: a common currency has just been created; ten new members are about to join the club; a convention on the future of Europe is under way, charged with writing the EU a draft constitution. You might expect all this to provoke a ferment of debate in Brussels. On the contrary, the tone of policy debate is generally cautious and technocratic. You will have no difficulty finding a seminar on inflation-targeting at the European Central Bank, or the formation of a European border guard. But the really fundamental questions tend to be avoided. The very novelty and fragility of much of what the EU is attempting seems actually to inhibit debate, rather than encourage it. With rare exceptions—for instance, the recent suggestion by the chairman of the European convention, Valéry Giscard d'Estaing, that Turkey is by definition unacceptable as an EU member—senior policymakers in Brussels, and the think-tanks that surround them, do not like to rock the boat.

Brussels, of course, is not Europe. In EU countries you do encounter real and fundamental debates about the direction of Europe. The British have a lively, detailed and seemingly never-ending debate about the euro. France has seen a much more anguished and wide-ranging argument than most other EU countries about whether or not EU enlargement is a good idea. Various senior German politicians have long questioned whether Turkey should join. There are powerful Eurosceptic parties in Denmark, Sweden and even, these days, the Netherlands. Yet these debates and arguments seem to be quickly stifled when they are brought up at headquarters. One commission official comments: “You do get people with funny ideas arriving in Brussels sometimes, but they usually become house-trained pretty quickly.” There are many examples of this process. Neil Kinnock, a former British Labour Party leader now vice-president of the commission, at one point in his career at home thought Britain should withdraw from the EU. Otmar Issing, now chief economist at the European Central Bank, used to be sceptical of the very idea of a single European currency.

The tendency to “go native” in Brussels extends well beyond officials and academics. Even the Brussels press corps is a pretty “on message” bunch, as becomes evident when its members venture out of Belgium en masse. On a press trip to Sweden in 2001, the Brussels scribes encountered a beast strange to them, Leif Pagrotsky, a cabinet minister—of a country that is a full EU member, after all—who seemed to be a Eurosceptic and who opposed the idea of Sweden adopting the single European currency. As the dinner conversation became increasingly heated, Mr Pagrotsky had a sudden insight: “I thought I was meeting journalists,” he said, “but it turns out that you are missionaries.”

The power of the Brussels consensus means that the convention on the future of Europe, whose duty it is to rethink the European Union from first principles, is in fact conducting its debate within tight intellectual boundaries. The fiercest controversy is between the advocates of the “community method” and the “inter-governmentalists”, with the former intent on building up pan-European governmental structures like the European Parliament and the commission, and the latter keener on fostering co-operation between national governments. Yet for all the heat that this debate generates, it is essentially an argument about different routes to the same goal, closer European integration. There are one or two delegates who seem to be willing to delve a bit deeper, but they are generally regarded as either mad or bad.

Can the EU connect with its people?

Decrying the absence of Eurosceptics in the policy debate in Brussels is in some ways unfair. It is a little like asking American policy wonks to start all discussions by first questioning the right of the United States to exist. The European convention would doubtless be more representative if it included more of the almost 50% of EU citizens who, according to the EU's own polls, would be either “indifferent” or indeed “very relieved” if the EU were to be scrapped. But it would also find it impossible to achieve consensus. The ability of Brussels to “house-train” newcomers is essential to creating the common assumptions that make agreement possible. But it also means that the European convention's underlying goal, to end the lack of connection between the EU and its people, is probably unachievable. That may become evident if and when a new constitution is tested in referendums across the Union.

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The establishment

The ascent of British man

Dec 5th 2002
From The Economist print edition

How things have changed at the top of Britain's professional ladder

TEN years ago, *The Economist* looked at how the educational background of the people in 100 top jobs in Britain had changed over 20 years. We found that almost the same number of people had been to public school (code for the smart private establishments which make up 450 of Britain's 4,300 secondary schools) and Oxford or Cambridge as in 1972 (see article from 1992). Now the results are rather different (see table).

What a difference ten years make
% of survey that went to...

	1972	1992	2002
Public school	67	66	45
Oxbridge	52	54	35

Source: *The Economist*

We chose 100 top jobs in politics, business, academia, the professions, sport and the arts. The list (see below) is necessarily arbitrary. Only the foolish will be offended by omission. As far as possible, we stuck to the list we used in 1992. Some change was forced upon us. There is no longer a governor of Hong Kong, for instance, and there is a mayor of London. Some companies have faded while others have grown, so we chose the chairmen of the 18 most valuable FTSE companies, plus those of the stock exchange and Lloyd's, to make up our business contingent.

The class of 2002

A selection of Britain's top people

Name	Position	Year of birth	Sex	Public school	Oxbridge
Gerry Adams	President, Sinn Fein	1948	M		
Edward Balls	Chief economic adviser to Treasury	1967	M	•	•
Percy Barnevik	Chairman, AstraZeneca	1941	M		
David Bean	Chairman, Bar Council	1954	M	•	•
Margaret Beckett	Environment secretary	1943	F	•	
Maarten van den Bergh	Chairman, Lloyds TSB	1942	M		
Tony Blair	Prime minister	1953	M	•	•
Sir Christopher Bland	Chairman, BT	1938	M	•	•
David Blunkett	Home secretary	1947	M		
Lord Blyth	Chairman, Diageo	1940	M		
Sir John Bond	Chairman, HSBC	1941	M	•	
Sir Albert Bore	Leader, Birmingham City Council	1946	M		
Richard Bowker	Chairman, Strategic Rail Authority	1967	M	•	
Sir John Boyd	Chairman of trustees, British Museum	1936	M	•	•
Sir Alec Broers	Vice-chancellor, Cambridge University	1938	M		•
Martin Broughton	Chairman, British American Tobacco	1947	M		
Gordon Brown	Chancellor of the exchequer	1951	M		
David Calvert-Smith	Director of public prosecutions	1945	M	•	•
Sir Graeme Catto	President, General Medical Council	1945	M	•	
Robin Cook	Leader of the House of Commons	1946	M		
Donald Cruickshank	Chairman, London Stock Exchange	1942	M		
Alistair Darling	Transport secretary	1953	M	•	
Sir Richard Dearlove	Head of MI6	1945	M	•	•
Iain Duncan Smith	Leader of the opposition	1954	M		
Greg Dyke	Director-general, BBC	1947	M		
Elizabeth II	Queen	1926	F		
Niall FitzGerald	Chairman, Unilever	1945	M		
Roderick Floud	President, Universities UK	1942	M	•	•
John Gardiner	Chairman, Tesco	1937	M		
Sir Edward George	Governor, Bank of England	1938	M	•	•
Anthony Giddens	Director, LSE	1938	M		
Ben Gill	President, National Farmers' Union	1950	M	•	•
Tony Hall	Executive director, Royal Opera House	1951	M	•	•
Patricia Hewitt	Trade and industry secretary	1948	F		•
Sir Christopher Hogg	Chairman, GlaxoSmithKline	1936	M	•	•
Geoffrey Hoon	Defence secretary	1953	M	•	•
Michael Howard	Shadow chancellor	1941	M		•
Paul Hyett	President, RIBA	1952	M	•	
Lord Irvine	Lord Chancellor	1940	M	•	
Sir Robin Janvrin	Private secretary to the queen	1946	M	•	•
Sir Michael Jay	Head of diplomatic service	1946	M	•	•
Digby Jones	Director-general, CBI	1955	M	•	
Charles Kennedy	Leader, Liberal Democrat Party	1959	M		
David King	Chief scientific adviser to the government	1939	M		
Neil Kinnock	EC commissioner	1942	M		
Richard Leese	Leader, Manchester City Council	1951	M		
Allan Leighton	Chairman, Royal Mail	1953	M	•	
Lord Levene	Chairman, Lloyd's of London	1941	M	•	
Helen Liddell	Scottish secretary	1950	F		
Ken Livingstone	Mayor of London	1945	M		
Sir Colin Lucas	Vice-chancellor, Oxford University	1940	M	•	•

The drop in the number of public school and Oxbridge alumni is most noticeable in business. Ten years ago, every company chairman on our list had been to public school and 12 had been to Oxbridge. Of the current list, eight out of 20 went to public school and four to Oxbridge. This is partly because of the arrival of foreigners such as Maarten van den Bergh at Lloyds TSB (Dutch) and Niall FitzGerald at Unilever (Irish). But it is also because there are more state-school educated Britons, such as Shell's Philip Watts and BAT's Martin Broughton, at the top.

Elsewhere, change is fairly evenly distributed. Among the political jobs in the survey, a few are held by public-school alumni—such as Tony Blair, Alistair Darling and Lord Irvine—and a few by Oxbridge types—such as Tony Blair, Patricia Hewitt and Michael Howard. Oddly, while the Labour Party is run by a product of the public school system and Oxbridge, none of the leaders of any of the other main political parties—Iain Duncan Smith of the Tories, Charles Kennedy of the Liberal Democrats, Gerry Adams of Sinn Fein and John Swinney of the Scottish National Party—have been to either. Mr Duncan Smith went to a cadet (military) school, which doesn't count.

Eighteen people didn't go to university at all—some because they went to military colleges, some because they came up through sports and the arts, and some (such as Michael Martin, speaker of the House of Commons and a former sheet-metal-worker) because they were poor boys made good.

The institution that has suffered most is Eton. It is down from 14 in 1972 to eight in 1992 to two—Charles Nunneley of the National Trust and David Calvert-Smith, the director of public prosecutions.

Among the things that haven't changed is the average age of the top people: 57 now, the same as it was in 1992. In 1972 it was 58. The only person who has been on all three lists is the queen (who didn't go to school at all, let alone university). The queen's private secretary, the ambassador to the United States, the boss of the Royal Opera House, the Master of the Rolls, the chairman of the Bar Council, and the spies are all still public school and Oxbridge chaps (or chapesses, in the case of MI5). But many other core establishment jobs have fallen. The BBC is now run by the determinedly demotic Greg Dyke, the Church of England by a leftish state-school product, Rowan Williams, and the *Times* by an Australian, Robert Thomson.

Perhaps the most startling result of all comes from the female contingent. Women's representation among the top people has risen by a massive 25%—from four to merely five. Twenty per cent of the present contingent are the queen.

As to the future, we reckon that the public schools will reassert themselves—because they have become fiercely academically competitive over the past couple of decades, and because the state system has got worse by comparison. Oxbridge will hold its own for a while, and then see its share shrink further, as the standard of higher education in Britain continues to decline and more and more students sign up for universities abroad.

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Accents

We want to talk proper

Dec 5th 2002
From The Economist print edition

Why so many British people are taking elocution lessons

NOW that Britain's public-school elite is in retreat, is the way it talks disappearing too? For years social levellers have been celebrating the decline of Received Pronunciation (RP), the clipped, cut-glass way of talking often known as Oxford, or BBC, English. Once the confident accent of the ruling class, it is now, supposedly, the dying dialect of an enfeebled tribe, attracting suspicion and contempt rather than deference and respect.

But it's not as simple as that. Certainly, RP, as it once was, no longer rules. The BBC goes out of its way to use regional accents; in Hollywood, a posh British accent is a cliché for brutality, arrogance and stupidity. Consumers no longer see it as a sign of trustworthiness and authority. Peter Trudgill, a leading socio-linguist, says that some call-centres prefer regional accents to RP because of the negative reactions RP arouses. Although there is little solid research, linguists think that RP speakers may have fallen from 5% of the population to less than 3%. “There may well be more RP speakers abroad than here,” says David Crystal, the country's best-known authority on the English language.

And RP has evolved. Today's version is closer to accents that once would have been termed plebeian. The Queen Mother spoke differently from the way her daughter talks. Princess Diana's speech was different again—closer to the generalised southern accent sometimes called “Estuary English”. Modern RP includes, for example, some glottal stops (an illustration is “Gatwick” pronounced without the “t”).

There is a large and growing demand for “better” speech

Yet—annoyingly for the egalitarians who believe that all kinds of accent are equally beautiful and useful—there is a large and growing demand for “better” speech. Ann Jones, the general secretary of the Society of Teachers of Speech and Drama, estimates that more than 10,000 people take elocution lessons every year. “In the last five or six years it's really taken off,” she says. Her members (who call themselves speech trainers, rather than elocution teachers, a term regarded as very dated) have as much work they want. The director of the London Language and Drama School, Sarah Mann, says that all speech training courses are fully subscribed, and some 200 people are paying £45 ($71) an hour for one-on-one coaching.

This is not a reprise of Shaw's “Pygmalion”. Most people signing up for lessons are not trying to learn classic RP, but to make their verbal skills match their other business tools—such as the visuals on a slide presentation. A typical aim is to soften or dilute regional accents to the point that they will be readily understood by people from elsewhere. Ms Mann says that it can take as little as six one-hour lessons to help a motivated student to replace glottal stops with “t”s in words like “water”, and to insert a missing “l” into words such as “old”, “cold” and “gold”.

She does not necessarily try to eliminate regional accents, she insists, so long as the speaker learns to eliminate “lazy” speech such as slurring, and annoying verbal tics, such as “know what I mean”, “sort of”, or “like”. “You can get away with even quite a marked accent if you are an interesting enough speaker, with pitch and pace and pause in your delivery,” she says.

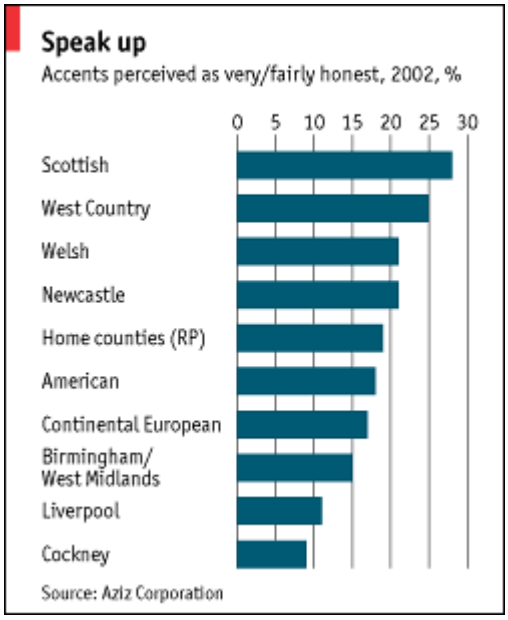
There is a strong business case for all this. A survey of company directors (see chart) by the Aziz Corporation, which calls itself the country's leading independent spoken communications consultancy, says that 31% reckon that a strong regional accent is a disadvantage in business.

But why the growth in demand? One reason is globalisation.

Foreigners typically learn RP, or something like it, and are often mystified by Britain's stronger regional dialects. Dealing with them means speaking some sort of standard English.

A second reason is the growing emphasis on better presentation skills in business. Managers who are willing to lavish money on public relations, speech writers, coaches and so on are more likely to want their Ps and Qs fixed too.

A third reason is the erosion of boundaries within companies. Jayne Comins, a speech coach in London, notices a big increase in clients with a computing background. “Talking's not what they are really about,” she says. “A lot of men in IT didn't start out wanting a job working with people, but when they become successful they often have to talk at board meetings, give presentations and sell their product.”



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Santa

Don't touch

Dec 5th 2002
From The Economist print edition

Panic about paedophilia is spoiling Christmas

EPA

One inch closer and I'll scream

THREE total strangers trying to give expensive gifts to a new-born baby? Highly suspicious behaviour. Even more so if another lot turn up accompanied by sheep, of all things. Goodness knows what the safety-maniacs would have made of the real Christmas. The latest example of paranoia is new guidelines on child safety in Santa's grotto, reluctantly issued by the country's Rotary Clubs (whose members spend a lot of the Christmas season doing good works, often dressed up as Santa). These say that a third-party adult (apart from the parent) must be present at all times.

> The arrangements must be such that there cannot be any possibility of Santa being placed in unaccompanied 'one-to-one' contact with a child in a 'private' place such as a 'grotto'

In addition, touching Santa is discouraged: children should shake hands or blow a kiss.

It is possible that paedophiles across the country are fuming that "grotto grooming" won't work this year. More likely, though, the molesters will continue their nasty behaviour just as before, and life for children has just lost another little slice of fun.

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University fees

Skinning the student cat

Dec 5th 2002
From The Economist print edition

How to get more money into universities

Get article background

FOR years, the proposal that universities should charge top-up tuition fees has been knocked about by policy-wonks in think-tanks. Now it's out in the open and it won't go away, despite protests from students and Labour backbenchers, and divisions between ministers, not least between Tony Blair and Gordon Brown.

Britain's universities are broke, lecturers are ill-paid and courses are overcrowded. More money has to be found but further recourse to the general taxpayer on the scale needed to rescue the universities is out of the question, given the huge sums already committed to health and schools. That leaves students themselves, who can expect higher earnings because of their university education.

But raising extra money for universities is not the government's only objective. Maintaining and if possible improving access for poor students is another priority. And Mr Blair and Charles Clarke, the new education secretary, are also keen to allow a greater role for market forces in higher education, so that universities can differentiate themselves to a much greater extent. The fear is that without such reform, Britain's top universities will slide inexorably down the world pecking order.

There are three main options for reform in the government's review of university finance, due in January. The first is to stick with the current system of tuition fees paid up-front by students but to increase them from their current means-tested level of £1,100 a year. The higher fees could either remain uniform or could vary from university to university. The snag with this proposal is that it would raise only a modest amount of money—even now only 40% of students pay the full amount—but could deter access. Mr Blair appeared to rule out the option this week when he said that reform would not mean parents having to pay thousands of pounds of fees up-front.

The second option, said to be backed by Mr Brown, is a pure graduate tax, which future graduates would pay for the rest of their working lives. This would certainly raise a lot of money, but it would leave a funding gap for several years until enough graduates were paying it. The open-ended obligation to pay higher tax could deter some people from going to university. And it would not make universities any more responsive to the market.

That leaves option three, which Mr Blair supports. This would allow universities to vary their fees, up to a cap of £5,000, but students themselves would not have to pay this up-front. Instead they would repay the cost once they graduated and started to earn enough. All students could be charged, so increasing the revenue compared with up-front fees. However, they should not be deterred from university since they would only have to make repayments of a fixed sum, unlike the graduate tax, and the system would offer protection to low earners. Universities would get their money immediately: “it is perfectly possible to have loans covering all the tuition fees and to raise the money from the private sector,” says Nicholas Barr of the London School of Economics. Since repayments would be made through the tax system, both Mr Brown and Mr Blair could claim victory. It is the most likely way of skinning the student cat.

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Scottish sectarianism

Bad old habits

Dec 5th 2002 | GLASGOW
From The Economist print edition

Ancient hatreds die slow

NEAR the centre of the Lanarkshire town of Airdrie there is a huge mural glorifying the victory of King William III over James II at the Battle of the Boyne in 1690, which expunged the Catholic monarchy from Britain. This sort of thing, all too understandable in Belfast, seems little more than an oddity in a Scottish town which history has pretty much ignored. Yet what it symbolises is worrying Scots.

This week Scottish ministers announced that prosecutors will have to tell courts if religious sectarianism is an element in a crime. Politicians are thinking of tougher sentences too. The most recent cause was a football match in October between the bitter Glasgow rivals, Rangers (mainly Protestant) and Celtic (mainly Catholic). Several people were stabbed and police made 37 arrests. A Rangers player says that sectarian abuse means he changes his phone number every week, and a Celtic player, Neil Lennon, quit his national team (Northern Ireland) because of death threats.

Concern had been rising already. In 1999 a noted Scottish Catholic composer, James MacMillan, publicly complained about “visceral anti-Catholicism”. A priest in a working-class area of Glasgow has had guns fired through his windows, firebombs thrown at his church and innumerable telephone threats. Even Scotland's first minister, Jack McConnell, has had Ulster paramilitary slogans daubed on his house in Lanarkshire. A survey by Glasgow council found that 12% of its citizens thought they had been victims of sectarianism at sporting events or when job-hunting. Two-thirds say religious tension is a significant problem in the city.

It is odd that this dismal historical hatred persists in Glasgow, but has been virtually eradicated in Liverpool. Both cities experienced large-scale Irish immigration in the 19th century, of both Catholics and Protestants. Both experienced anti-Catholic riots in the early 20th century, and local politics and employment in both cities were riven by sectarian factionalism.

In 1966, two new church leaders arrived in Liverpool, Anglican Bishop David Shepherd and the Roman Catholic Archbishop Derek Warlock, and embarked on an ecumenical crusade, including a “walk of witness” between their two churches.

Getting that kind of popular campaign going in Scotland, however, may be much more difficult. Bronwen Walter, an academic specialising in the Hibernian diaspora, says Irish immigrants to Britain have mostly felt compelled to keep quiet about their identity, the more so in recent years because of Ulster's sectarian conflict. Supporting Celtic is an outlet. Rangers fans, on the other hand, may have reacted to the strengthening Scottish identity by intensifying their prominent display of British symbolism such as the Union flag.

But the churches are now doing more. Mario Conti, recently arrived from Aberdeen as the Catholic archbishop of Glasgow, says he is shocked at the level of intimidation his flock experiences; he hopes to use a church anniversary next year for more ecumenical work. Alan D. McDonald of the Church of Scotland agrees: “For years we denied its existence, but the demon is out now.”

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Drugs

User friendly

Dec 5th 2002
From The Economist print edition

The government hopes treatment will get Britain off drugs

DRUGS are dirt cheap—a heroin fix costs less than a cinema ticket—but their social and economic cost is estimated at between £10 billion and £18 billion a year. For years, the government has relied on tough penalties to stop the growth of drug use. They haven't. Now the emphasis is shifting to curing junkies instead. Tony Blair wants to double the number of addicts in treatment by 2008, bringing the total to 200,000, or nearly four in five problem users, and to boost government spending on treatment services from £438m to £573m.

The publication this week of an “updated” drug strategy highlighted both the usefulness of a treatment-based approach and the difficulty of extending it effectively. Treatment makes sense. It has more impact than punishment on levels of drug use, and so on health, life expectancy and crime levels. Every pound spent on treatment returns more than £3 through savings in the criminal-justice system.

Earlier this year, however, the Audit Commission reported that treatment services are so badly co-ordinated that they fail thousands of addicts. Waiting times can run to six months. Two-thirds of GPs say they lack the expertise or back-up to support users. Some local authorities refuse to stump up for residential treatment, which is expensive but works better than community care. Last year an agency was set up to address these problems and to organise drug treatment at a national level.

While providers welcome the government's commitment to treatment, they worry that the extra money is not reaching the front line. State funding of residential treatment, says Tristan Millington-Drake, chief executive of the Chemical Dependency Centre, a charity and treatment provider, remains a serious problem. For the client, finding state money for treatment means slogging through jungles of red tape, while for the provider, that money covers just two-thirds of the full cost.

The shortage of skilled drug workers is another big concern. The government hopes to attract 2,000 new workers by 2006, but providers reckon the number required is more like 4,000-5,000. Finding people to do those jobs will not be easy. Nobody goes into the treatment business for the cosy conditions, the enviable salaries or the sparkling chit-chat.

Many of the best drug workers are former users

Many of the best drug workers are former users. Recovering clients see hope for themselves in the example of a reformed addict turned counsellor, says Adam Sampson, chief executive of the Rehabilitation for Addicted Prisoners Trust (RAPT), which offers treatment in prisons. The importance of this relationship comes across clearly during a RAPT group-therapy session at Wandsworth prison, in south-west London. The connection between the prisoners and the two counsellors guiding the session is obvious. Without it, it is hard to imagine a group of convicted criminals sitting down to talk freely about their painful family lives, their romantic entanglements and other factors behind their addictions.

Mr Sampson acknowledges that in some respects it is easier to provide effective treatment in prison than it is in the community. There is a captive audience, and denial is more readily overcome, since the evidence that the combination of drugs and crime can get you into trouble is inescapable. No doubt these factors contribute to RAPT's impressive success rate.

But what works in prisons should also work in the community. It depends, Mr Sampson says, on flexibility and responsiveness to individual needs, seeking out the best possible counsellors and closely monitoring clients from the moment of referral through tailored treatment to follow-up. These are all, he admits, pretty basic principles. But those basic principles—and realistic funding—are essential to any

successful treatment programme.

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Fox-hunting

Foxed

Dec 5th 2002
From The Economist print edition

The government wants a compromise on hunting. Its MPs don't

Left hanging

AFTER more than five years and nearly as many votes to ban fox-hunting, the government has finally said what it thinks should happen. Sort of.

The bill it has laboured so long to produce could not have been better calculated to make almost everybody cross. As such, the wretched minister for rural affairs, Alun Michael, in whose lap the mess has landed, can at least claim it to be a perfect example of the "middle way". Although the government is clear that it wants to get rid of some forms of hunting with dogs—hare coursing and stag hunting have definitely had it—it is more ambivalent about fox-hunting, despite the determination of most Labour MPs to get rid of that too.

To that end, it has suggested a form of licensing, under which a national registrar would decide which hunts were the most efficient and least cruel form of pest control available. This raises the possibility of hunting being permitted in some places, and a criminal offence in others.

Mr Michael has made an heroic, if doomed, attempt to trace what he calls a "golden thread" through every aspect of a complicated subject that takes in land management, species conservation and vermin control. He has endeavoured to do this for good reasons. While the government is blind to the threat to civil liberties, it is worried about clogging up the courts and wasting police resources by making criminals out of previously law-abiding citizens. It is also more aware than it was of the economic and social impact of banning hunts in parts of the country where farm incomes are already declining.

It is no less concerned about the potential for parliamentary paralysis should the House of Lords throw the bill out, an outcome that would have been invited by a straightforward prohibition on hunting in all its forms. Ministers have long regretted the consequences of Tony Blair's uncharacteristically rash promise three years ago to settle the matter once and for all.

Unfortunately, despite Mr Michael's efforts and attempts by the Labour whips to convince angry anti-hunting MPs that few hunts will survive the bill's rigours (the government has, naturally, told the pro-hunting Countryside Alliance the exact opposite), the golden thread looks almost certain to unravel. The anti-hunt MPs have a large majority and, invincible in their moral certainty, intend to wield it. The question then will be whether the government has the cheek to use the Parliament Act to force through such a fundamentally amended bill. It probably will.

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Bagehot

A dangerous game

Dec 5th 2002
From The Economist print edition

The differences between Gordon Brown and Tony Blair are an odd mix of the synthetic and the real

AT WHAT point does “creative tension” turn into something more destructive? It's a question that Gordon Brown should ask himself. While differences between the chancellor and Tony Blair are not exactly new, Mr Brown has recently become bolder in advertising their extent and nature. He may not quite have done so yet, but he is getting perilously close to stepping over the line where legitimate argument ends and direct challenge to the prime minister's authority begins.

When the Blair-Brown relationship is going through one of its bad patches, their proxies let the world know. These people have been as active as usual during this round, insisting things between the two men have “never been worse” and that there have been “blazing rows” after which they are “not speaking”. But this time, there is an important difference. Over-enthusiastic subordinates, even if they are only doing their master's bidding, can be disowned. But when the chancellor appears to be declaring his opposition to the prime minister directly and more or less publicly, the game has changed—and become more dangerous.

Mr Brown's rampage began a few weeks ago when he told journalists from the *Guardian* newspaper over breakfast that the university top-up fees (which Mr Blair is supposed to favour) are “a ridiculous idea”, thereby giving encouragement to other dissenters. Then, in a speech last week, he talked about “recognising the limits to markets” in health care and education. This was widely interpreted as a coded rebuke to the prime minister for his growing determination to encourage new forms of provision of services, and of competition between service providers. In the course of his pre-Budget report, he implicitly made an unflattering comparison between the monetary and fiscal regimes for the euro and his own policy framework. Simultaneously, he allowed the publication of a Treasury paper that poured scorn on the very idea of fixed exchange-rate regimes—hard to square with the prime minister's continuing insistence that joining the euro is “our destiny”.

Of these rumbling arguments, the one over the euro has generated most excitement, closely followed by the more recent spat over the matter of finding a solution to the chronic under-funding of Britain's universities. It is the dispute over higher education that is the more serious, though not for the reasons that most people think.

It is the dispute over higher education that is the more serious

Over the euro at least, there is really nothing to fight over, because, as Mr Brown's economic adviser, Ed Balls, suggested in a mildly conciliatory speech this week, both men are right. It would indeed be folly not to insist on a rigorous evaluation of the economic consequences before joining the monetary system. Nor is it the chancellor's fault if the unintelligent application of the euro zone's crude rules have, for now, reduced any chance of winning round the sceptical (and very constant) two-thirds majority in Britain who oppose euro entry—although Mr Balls bullishly claimed a referendum could still be won if the economic tests were met. At the same time, Mr Blair has good grounds for fearing that Britain's influence in the EU will decline if other countries write off the prospect of its ever signing up. Still, having given Mr Brown a de facto veto on the euro, Mr Blair should accept it with good grace. The euro, in truth, is quite probably not for this parliament, but for the next. And, as such, it is not worth falling out over.

In one respect, the row over top-up fees has also been over-blown. A meritocrat like the chancellor cannot plausibly subscribe to such an extreme form of egalitarianism that he would happily preside over the slow destruction of Britain's best universities, nor can someone who exults in the collective brainpower of the Treasury deny that there's a place for intellectual elitism. The notion that Tony Blair is content to make Oxford and Cambridge the preserve of the wealthy by frightening away able students of

modest means is even more ludicrous.

The trouble is that even if both agree that they want excellent universities which children from all backgrounds can go to, it doesn't follow that there's any consensus about how to get there. Mr Blair believes it is necessary to give universities greater freedom to set tuition fees so they can differentiate themselves in a global market. Mr Brown wants the state, rather than the universities, to collect and disperse the money, perhaps through a graduate tax. By retaining control, the state will be able to prevent a hierarchy of rich and poor institutions emerging.

A little local difficulty

The eventual solution to the universities' problem will probably ultimately be driven more by fear of middle-class anger than by ideology. But that does not detract from the philosophical importance of the divide, which cuts across the entire canvas of public service reform. Mr Brown is as determined as anyone to see working practices in the public sector modernised, as his unyielding stance towards the firemen's strike has demonstrated. But he regards Mr Blair's criticism of the way the government has so far attempted to get results—by setting targets and minutely measuring inputs and outputs—as a thinly-veiled attack on himself. He believes that Mr Blair's new emphasis on local autonomy and "contestability" (New Labourese for competition) is a cover for a neo-liberalism that is at odds with the traditional Labour concern for equality of provision—hence the rows over foundation hospitals and radical ideas about state-funded, but independent, schools.

Unlike the euro, these are serious arguments worth having. But they are potentially lethal if conducted in the wrong way. Which is why Mr Brown's present modus operandi is so fraught with danger. Mr Brown must understand that in any government there is room for only one prime minister. Which, of course, is also what this is all about.

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An uncertain giant

Dec 5th 2002
From The Economist print edition

AP

Germany is plagued by a severe economic malaise and by uncertainty about its place in the world, says Xan Smiley

AT THE heart of Germany's old-new capital, Berlin, a heady mixture of symbols confronts the visitor. Start with the Reichstag, restored as the unified nation's parliament: a ponderous Prussian hulk of a building with an awkward history, renovated and now capped with a delicate glass dome, proclaims a peculiar yet suitably mixed message of old solidity and adventurous novelty.

Then look across to the Brandenburg Gate, a mocking reminder of Germany's division that until 1989 stood gloomily alone in the border wasteland near the site of Hitler's old bunker. Now that it has been restored, the horse-drawn chariot on top of the majestic gate seems poised to take off eastwards into territories soon again to fall within Germany's economic embrace.

And the bunker itself, a place that most Germans would rather expunge from their capital, if not from their historical memory? The country's leaders have courageously decided to erect, close to the site of the bunker, a massive and eerie memorial to a crime that must not be forgotten, however normal Germany has now become and however blameless today's Germans are for the appalling crimes committed by their grandparents.

On the face of things, Germany has finally come out of its post-war shell. Twelve years ago it emerged united, suddenly much more populous and with a far bigger economy than its chief counterparts in Europe—although, by taking in the poor east, it became less wealthy per head. It now has 82m people, against about 60m each for France and Britain, which makes it the undisputed giant at the heart of one of the two richest continents in the world. The European Union has 370m people against America's 270m, and a combined annual GDP of $7.9 trillion against America's $10.1 trillion. In little more than a year's time, if the 15-country EU expands as expected to take in another ten countries, mainly in Central Europe, the Union's population will rise to 460m. Hence the symbolism, once again, of moving Germany's capital in 1999 from the sleepy little Rhineland town of Bonn, a mere 55km (34 miles) from the border with Belgium, to raucous, once-imperial Berlin, just 80km from the frontier with Poland.

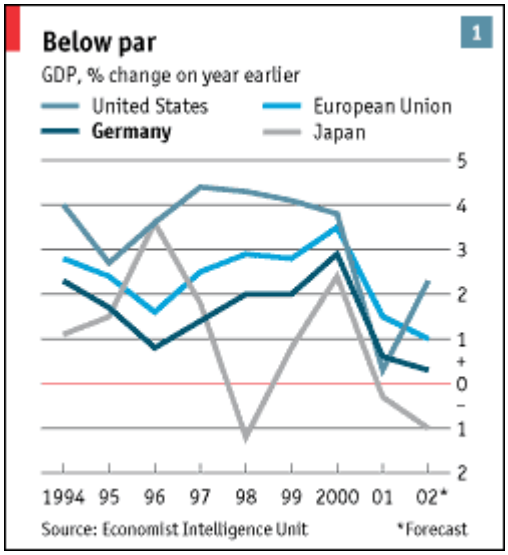
Look east

The shift in Germany's centre of gravity to the east has been accompanied by the departure of French, British and Russian troops from German soil, and by the reduction of once-mighty Russia to the economic weight of the Netherlands. Moreover, the burgeoning European club of which Germany is the biggest member will soon embrace Poland and three Baltic countries that not so long ago seemed an integral part of Russia's empire.

Yet just as Germany seems to be retaking its place at the head of Europe's top table of nations, there is growing concern (in Germany as well as abroad) about a “German malaise”—mainly of an economic kind, but also reflecting uncertainty over how the country might play its part on the European and global stage. The chancellor, Gerhard Schröder, recently won an extremely narrow election victory, which he owes partly to his decision to thumb his nose at the government of the United States, a country whose friendship has been the cornerstone of German foreign policy for half a century. Germany's equally important post-war friendship with France has also fallen into disrepair, although efforts have recently been made to restore it. A third friendship, with Britain, seemed to be taking root two years ago, but never quite flowered.

In sum, for the first time since the second world war, Germany has given the impression of wanting to carve out a more independent place in world affairs for itself—but it does not yet seem to have worked out what to do with it.

Germany's economy remains easily the biggest in Europe, larger by a third than Britain's or France's. But the mighty American economy is now five times as big as the German one, against 3.7 times in 1990, and the gap is widening. For the past eight years, the German economy has been the slowest-growing in the whole of the European Union, so in comparison with its peers it has lost ground (see chart 1). Recently, Germany has suffered the indignity of being formally reprimanded by the EU for letting its deficit get too big.



True, in 1990 it was landed with the colossal financial burden—however welcome politically—of absorbing a bankrupt country, the former communist-run German Democratic Republic. True, Germany's is an export-driven economy gasping for breath during a world economic slump. But it is also stifled by a hugely restrictive and intrusive web of regulations, and weighed down by one of the most expensive, inflexible and protected labour forces in the world.

Fading lustre

Many of Germany's greatest firms and institutions are in trouble. All of its four biggest banks—Deutsche Bank, HypoVereinsbank, Commerzbank and Dresdner Bank—require drastic and urgent restructuring. When in 1999 Germany committed itself to surrendering its beloved D-mark, the symbol of post-war stability, in favour of a new European currency that now embraces 12 out of the EU's 15 members, there was much talk about Frankfurt ousting the City of London as Europe's financial hub (Britain having stayed out of the project). But in the past few years the DAX index of Germany's top companies has slumped even further than the stockmarkets in New York, London and Paris, and Frankfurt's much-vaunted *Neuer Markt* for high-tech shares, having lost 90% of its value in the past two years, is closing as a separate market early next year. In the past couple of years, Germany has been shocked by formerly rock-solid companies going bust.

Germany's once well-regarded education system, too, has lost its lustre. When the OECD last year published the results of its Programme of International Student Assessment (PISA) on the attainments of 15-year-olds in 30 rich countries, Germany came an embarrassing 21st, suggesting, among other things, that the famously high quality of Germany's shop-floor workers may soon start to fall.

Even standards of public morality and civic virtue seem to be declining. A few years ago a party slush-fund scandal tarnished the name of Helmut Kohl after 25 years at the head of the Christian Democrat party, 16 of them as Germany's chancellor. In the past couple of years a rash of scandals involving all the main parties has erupted. And note that Transparency International, a Berlin-based body that rates countries according to the cleanliness of their public ethics, puts Germany in 18th place in its latest league table, one rung below Chile.

Most German politicians these days intone in unison that “we need reform”, but few seem to recognise how urgent and radical it has to be if their economy is to regain its old fizz. Before the election in September, neither of the two main parties—Mr Schröder's centre-left Social Democrats and Edmund Stoiber's conservative combination of Christian Democrats and their Bavarian sister party, the Christian

Social Union—dared promote any ideas that might rattle the country's comfortable consensus. In the eyes of Anglo-Saxon-minded free-marketeers, the Germans are simply in denial, their government “sleepwalking into stagnation”.

But why worry?

Many Germans, on the centre-right as well as the centre-left, think their laisser-faire critics are exaggerating. Carpers have been saying much the same thing for decades, yet Germany remains a rich and comfortable country that treats its old, its sick and its unemployed far more generously than does, say, America or Britain. “Germans live very well. We have a fantastic welfare system,” said Alfred Tacke, a confidant of Mr Schröder in the economics ministry. “Our infrastructure is fantastic. Our workers have six or even eight weeks' holiday a year.” The Americans, he says, work about 25% more hours in a year. So what, he seems to be implying, if Germany drops a few places in those league tables of growth and productivity?

He has a point. For quality of life and protection of the weak, his country remains at the top of the league. Its welfare system is enviably generous. Its environmental and health standards are high. Its sense of civic virtue, despite that rash of corruption scandals, remains pretty solid. Public discourse is vigorous but dignified. Germany is an eminently civilised country with a solidly entrenched democracy. It threatens nobody. The ghosts of Hitler have been laid as well as they can be. If compromise and consensus slow down growth but deliver civil serenity, then let us—say many Germans— pay the price.

But the price could well rise. Some demographic projections suggest that, without net immigration on a grand scale, Germany's population could shrink from 82m today to about 60m, the same as France's and Britain's, within 30 years. That would make public pensions and health care at their present level unaffordable.

In his first term of office, Mr Schröder started some reforms, albeit tentatively, in several important areas: taxation, labour-market law and pensions. But as election day approached, they slowed to a halt. As Mr Tacke observed, “Reformist programmes don't win elections.” Now that the chancellor is back in the saddle for the next four years, will he become more reform-minded again? The first place to look for an answer is German politics.

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The perils of pragmatism

Dec 5th 2002
From The Economist print edition

Gerhard Schröder is a brilliant tactician. But where's the strategy?

KATS

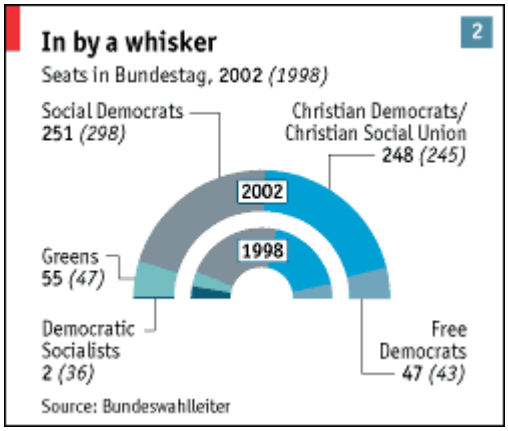
Is Schröder losing his grip already?

SINCE his narrow election victory, Mr Schröder has sorely disappointed his party's would-be modernisers and the dwindling number of businesspeople who think he can turn Germany's fortunes round. A hopeful early sign was his appointment of Wolfgang Clement, until then premier of North Rhine-Westphalia, Germany's biggest *Land* (state), to run a beefy "super-ministry" for economics and labour. But his new team as a whole looks no keener to ram through radical reforms than the previous one.

Mr Schröder's dismal post-election performance and apparent lack of stomach for forging boldly ahead have cast reformers into gloom. Many Germans who voted for him feel betrayed. Astonishingly, within two months of his victory, pollsters were already putting his Social Democrats 14 percentage points behind the Christian Democrats and their Bavarian allies.

In retrospect, the chancellor must consider himself extremely lucky to have held on to his job at all. In mid-summer, his chances seemed to be ebbing away. He had patently failed to keep the biggest promise he made to the German people in his first term of office—that he would bring unemployment down from 4m (around 9% of the workforce) to below 3.5m. It did come down at first, but for the past year it has been hovering around 4m again. Last spring Mr Schröder's Social Democrats were running up to ten points behind the opposition, led by Edmund Stoiber, the worthy, socially conservative premier of prosperous Bavaria.

The chancellor was saved by a string of what turned out to be lucky breaks, and squeaked home by polling just 6,000 votes more, in an electorate of 61.4m, than the conservative combination of Christian Democrats and their Bavarian sister party, Mr Stoiber's Christian Social Union. The first break came with the terrible floods of August, when the Elbe river and its tributaries ravaged Saxony's heartland and other parts of the east. Mr Schröder seized the moment, using his fabled charm to persuade the beleaguered easterners that he was their friend. He offered cash, comfort and a spirit of national solidarity. Mr Stoiber remained near-invisible.



Mr Schröder's second break was the growing threat of war in the Middle East and the apparent readiness of President George Bush to fight Iraq. Today's Germans are reluctant warriors, and the chancellor sensed that the mood was against the Americans. He may have genuinely believed, along with some other European leaders, that America's approach was wrong, even if it got a United Nations mandate, but to insult his country's most generous and steadfast post-war ally was patently self-serving.

The third break was inadvertently provided by the Free Democrats (FDP), Germany's liberals, who might have made a coalition partner for either big party but seemed more likely to team up with the right. Earlier in the year, pollsters said they might pick up as much as 12-13% of the vote, a lot more than the Greens, Mr Schröder's often awkward partners in the ruling coalition. But Jürgen Möllemann, then a deputy chairman of the party and its boss in North Rhine-Westphalia, got embroiled in a row over his outspoken pro-Palestinian views and alleged anti-Semitism. This made many Germans queasy. Suddenly the prospect of the liberals taking the foreign ministry, as they had done in several earlier coalitions, seemed fraught with risk. Liberal support slipped.

At the same time, the Greens benefited from the popularity of their unofficial leader and Germany's incumbent foreign minister, Joschka Fischer, as well as from fears of war and ecological worries stirred up by the floods. On election day, they gained 8.6% of the vote against the liberals' 7.4%. With the two main parties finishing neck and neck, with 38.5% of the national vote each, that margin was just enough to ensure that the Greens would be a stronger partner for the centre-left than the liberals would be for the centre-right.

Moreover, the defects of Mr Stoiber, the conservative challenger, became plainer as the campaign wore on. The then 60-year-old Bavarian Catholic, with his rasping, schoolmasterish speech, came over as stiff and old-fashioned. He lacked his 58-year-old rival's easy rapport, relaxed manner and deep-throated eloquence. Despite his model family life, he got far fewer women's votes than the four-times-married chancellor. And in eastern Germany, Mr Schröder cleaned up.

That Mr Schröder is a masterly campaigner and a shrewd tactician is not in doubt. He can also be courageous, as he was when he sent German troops to Kosovo in 1999 and to Afghanistan last year. And he notched up some creditable achievements during his first four years in office. He introduced bold and sensible tax reforms, encouraged people to start making private pension provision, and gave immigrants a better deal by making it easier for them to get German nationality. Indeed, by mid-term, Mr Schröder had begun to look good. The economy started to pep up and unemployment dropped.

Steady as she goes

But about 18 months ago Mr Schröder stopped being bold and started to reinvent himself as a helmsman with a steady hand on the tiller. He gave new perks to the trade unions. When Germany's economy began to dip again, he seemed at a loss; then, last spring, he asked Peter Hartz, an old friend from his days on Volkswagen's supervisory board, quickly to draw up a report on improving the labour market. In July Mr Hartz suggested a number of sensible ways to get more people into work, which Mr Schröder promptly embraced.

The trouble with Mr Schröder is that he is a pragmatist, not a radical reformer. He enjoys power, but he also likes to be liked. His earlier reputation as a moderniser rested largely with his closeness to big business, particularly VW, when he was premier of the state of Lower Saxony. But he is also a creature of the cosy corporatist consensus that served his country so well in the early decades after the second world war. “We Germans do not believe in big bangs,” says one of his closest advisers. In particular, Mr Schröder does not believe in fighting against Germany's still-powerful trade unions, who are understandably reluctant to loosen up the labour laws.

To be fair to him, if the conservatives had been returned to power, they would probably not be doing much better. After all, it was conservative governments, as much as centre-left ones, that have been responsible over the years for Germany's high taxes and the steady rise in its labour and social-security costs. Mr Stoiber himself has a record of intervention and deal-making with companies and trade unions in Bavaria. Germany's only truly free-market party are the liberals, who in a coalition with the conservatives might have made a difference, but probably not much.

But then Germans as a whole do not really believe that a crisis is afoot. Indeed, that was the message they conveyed by voting as they did in September. “We are not like Britain in 1979,” is a regular refrain, usually followed by the assertion that the measures applied by Britain's then prime minister, Margaret Thatcher, would not be suitable for their own country anyway. In Germany, compromise and consensus remain the order of the day. But can they still deliver the goods?

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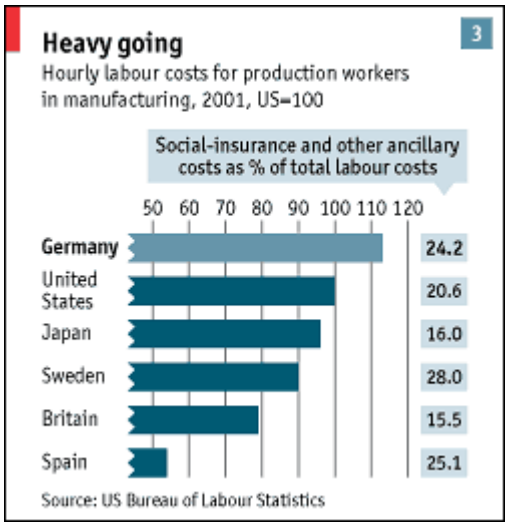
Is Deutschland AG kaputt?

Dec 5th 2002
From The Economist print edition

What's ailing German industry

CAN this really be the country of the *Wirtschaftswunder*—the economic miracle that brought burgeoning growth to Germany from the end of the second world war to the mid-1980s? Since the post-unification boomlet ended in 1994, growth has averaged only 1.6% a year, the lowest rate in the European Union; this year, says Wolfgang Clement, the new economics minister, the figure may be only 0.5%; some government advisers predict even less. Foreign direct investment into Germany has been paltry, and virtually all of Germany's biggest firms are setting up plants abroad to make products more cheaply. Bankruptcies this year are a third up even on last year's record.

The hourly cost of labour in manufacturing industry in western Germany, including wages, social-security (including health) and pension contributions, is 13% more than in America, 43% more than in Britain and 59% more than in Spain, according to the US Bureau of Labour Statistics (see chart 3). Yet Germany's once-admired productivity no longer outstrips its main rivals'. And although Germany has increased its exports (and is still the world's second-biggest exporter), those of other countries have grown faster. Its global share has dipped from 11.8% in 1992 to an estimated 9.7% in 2002.



When Germany agreed to swap its cherished D-mark for the euro, it hoped that the move would do its financial markets a power of good. It didn't. Indeed, the country's banking system is now in crisis. In the past few months, Deutsche Bank and Dresdner Bank have announced lay-offs, of 14,500 and 11,000 people respectively. HypoVereinsbank, Germany's second-biggest bank, has watched its profits dwindle and expects to make loan-loss provisions of *euro*3.3 billion for this year. Rumours of a liquidity problem have swirled around Commerzbank.

A merger between Deutsche and Dresdner failed miserably two years ago, and the marriage of Dresdner to Allianz, a Munich-based insurer, has been a flop. Plans two years ago for Deutsche Börse, which runs Frankfurt's stockmarket, to take over the London Stock Exchange ended in a mess, and Frankfurt's *Neuer Markt* for high-tech shares is to close soon after less than six years in business. Talk of Frankfurt taking over from the City of London as the hub of European finance has evaporated. Investment banking, in particular, has floundered as its big banks have failed to consolidate or expand. “We completely missed the boat,” says a leading Frankfurt investment banker.

The Germans have been dismayed suddenly to find their firms vulnerable to hostile foreign raiders. The takeover two years ago of Mannesmann, an engineering-cum-mobile-phone giant, by a British firm, Vodafone AirTouch (as it was then called), was a heavy psychological blow to German corporate pride. Mr Schröder at first tried to resist the takeover but eventually accepted the inevitable. “Goodbye, Germany AG,” said Rolf Breuer, then head of Deutsche Bank.

Bestriding the world or doing the splits?

Two years ago, a German business journalist, Werner Meyer-Larsen, wrote a book called “Germany Inc: The New German Juggernaut and its Challenge to World Business”. A new era, he wrote, had started in 1998 when Daimler-Benz bought America's Chrysler, and he cited a number of other examples of German firms “thinking big” and “going west”.

Deutsche Bank bought New York's Bankers Trust. Bertelsmann, a German publisher, bought Random House, the biggest American book-producer. Holtzbrinck, the owner of some weighty newspapers, bought three leading American publishers. Hoechst, a Frankfurt chemicals company, teamed up with a big American rival, Marion Merrill Dow, before merging with its biggest French one, Rhône-Poulenc, to become Aventis. Munich-based Allianz, Europe's biggest insurance company, had already bought America's Fireman's Fund. And Europe's Airbus, in which DaimlerChrysler's subsidiary, DASA, is a partner, had become Boeing's biggest competitor.

But Mr Meyer-Larsen may have got a little carried away. For sure, the DaimlerChrysler deal marked a striking international advance for German business. Daimler-Benz's boss, Jürgen Schrempp, the nearest thing to a business hero in Germany, seemed to be working wonders. But the business climate has got tougher, and a few years on several of those other link-ups look less triumphant.

Rex

VW's strength is its flexibility

In any event, many of Germany's firms remain small by international standards. Of the world's biggest 500 companies in market capitalisation, 238 are American, 50 Japanese, 36 British, 29 French and only 21 German.

One reason why Germany's biggest firms, such as VW, stand up to world competition is that they invariably have special deals to keep their workforces flexible. For example, the number of hours worked at Wolfsburg, VW's biggest plant, which employs over 50,000 workers, varies hugely according to the state of the market. At VW and elsewhere, millions of workers, in return for a shorter average working week, have been moving to new systems of “task fulfilment” rather than having to work a certain number of hours.

Mittelstand mutterings

The country's *Mittelstand* of small and medium-sized firms enjoys less flexibility. Many of these firms would love wage bargaining to be done at company level, not—as is usual—in nationwide bargaining with one of the giant trade unions. But most of the leeway, they feel, is on the other side. For instance, it is easy for workers to report sick, and they often do. The director of one chamber of commerce notes wrily that illness strikes selectively: 70% of the time, he says, on a Monday or a Friday. When workers are sick, they get full pay for six weeks. *Mittelstand* managers suggest that sick pay should start at 80% of the full wage, and drop with a prolonged absence.

Another source of irritation is the right of any employee to move from full- to part-time employment, whether it suits the employer or not. This discourages firms from hiring young women who might suddenly demand time off to look after a baby. Such provisions hit smaller companies much harder than big ones.

Yet another *Mittelstand* gripe is that Germany's high income-tax rates hurt the *Mittelstand* more than bigger firms because, being almost all family- or trust-owned, they tend to distribute profits in the form of higher pay. Mr Schröder's cut in corporation tax was more generous than that in income tax—yet another reason why many *Mittelstanders* complain that the chancellor is friendly to big business but instinctively hostile to smaller capitalists like themselves.

Another big *Mittelstand* headache is raising credit. The big banks, they say, are unhelpful. The banks deny this, but the sort of *Mittelstand* companies they deal with tend to be at the top end of the scale. A score of companies that arguably qualify for the *Mittelstand* category (because they are unlisted, and owned by families or foundations) have a turnover that exceeds *euro*1 billion. These substantial *Mittelstand* companies include such famous names as Miele (white goods), Behr (air conditioners), Stihl (chainsaws) and Trumpf (laser-cutters), which each have a turnover of between *euro*1 billion and *euro*2 billion and employ between 5,000 and 15,000 people. It is further down the ladder that Germany's banking system is proving inadequate to satisfy the *Mittelstand*'s thirst for credit.

Germans who prefer to be self-employed so that they can avoid paying salaried workers' full social-security contributions also complain that the dice are loaded against them. For example, lorry drivers who work on contract for a single company have been told that under new rules they count as part of the firm for which they deliver, adding 41% to the cost of employing them. As a result, a lot of freelance

Polish truckers are now distributing goods at a cheaper rate, taking jobs from their German counterparts. In a similar vein, the director of Hanover's chamber of industry and commerce, Wilfried Prewo, points out how much harder it is to become a taxi-driver in Germany than, say, in the United States. “Our logic is that you must always, if possible, be an employee,” he sighs.

Berthold Leibinger, the doyen of Trumpf, a classic *Mittelstand* firm based in Stuttgart, is another critic of restrictions that hamper entrepreneurship. “The Social Democrats don't understand the role and importance of the *Mittelstand*,” he says. “They're not pragmatic.” They're particularly hostile, he says, to people who inherited their firms. “We've become a safety-crazy nation,” he says. “We need to be more risk-minded. It's unbelievable that in two generations we've moved from a country that wanted to cover the world [in business] to one that is afraid of itself.”

According to an old joke among *Mittelstanders*, Bill Gates could not have made his fortune in Germany because it is illegal to turn a garage without a window into an office. Ah well, the jest goes on, Mr Gates would at least have ended up as a senior manager in a big corporation. But no: large German companies rarely give good jobs to university drop-outs.

Old-fashioned virtues

With so much to complain about, how do so many German firms still manage to do so well? The answer lies in good old-fashioned hard work, efficiency, attention to detail and precision, pride and high standards, particularly in engineering. In that respect, another part of the corporate tradition of German business, the apprentice system, still works well: newcomers join firms at token pay, usually for three-and-a-half years, and spend a day or more a week undergoing formal training elsewhere at the expense of the state—and then, if the firm likes them, join as full-fledged and often very loyal staff members.

Many leading businessmen—including Josef Ackermann, the (Swiss) new Deutsche Bank boss, Paul Achleitner, Allianz's (Austrian) chief financial officer, and Gerhard Cromme, head of ThyssenKrupp's supervisory board—are known to be frustrated by the German economy's over-regulation. Their calls for a less restrictive regime may gradually be heard. Many of the new wave of Germany's top businessmen have had experience in the United States, and feel that degrees in business management (such as those now offered by the Stuttgart Institute of Management and Technology, and by the European School of Management and Technology founded in Berlin in October) should be much more widely available in Germany.

“For the past ten years we haven't been moving,” says Hans-Olaf Henkel, a former head of IBM in Germany and for a time a notably outspoken head of the Federation of German Industry (BDI). Like other go-ahead businessmen, he recites a litany of measures that would help to free the economy but concludes gloomily: “The political will just isn't there.”

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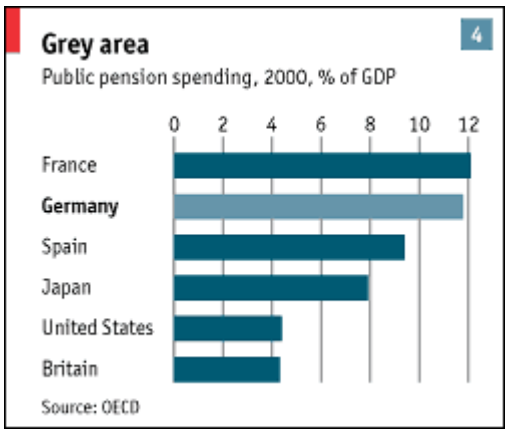
Loosen up or lose out

Dec 5th 2002
From The Economist print edition

Germany has far too many rules and regulations

MOST analysts readily agree on what is wrong with the German economy. First and foremost, the labour market is far too sticky. Second, taxes and social-security contributions are too high and profits too low. Third, and not unconnected, social-security payments, pensions and health-care arrangements are too generous. And fourth, there is far too much red tape. Frustrated businessmen often say that in English-speaking countries everything is allowed unless specifically forbidden; in Germany, it is the other way round.

Mr Schröder made a useful start on tax reform in his first term by cutting corporate taxes from 52% to 39%. He also initiated a step-by-step reduction in income-tax rates, starting in 1998. The top rate was due to fall from 53% to 42% by 2005, though he decided just before the election to delay the latest scheduled cuts by a year, to help pay for flood damage. One of his more far-sighted reforms—which, to their shame, was opposed by the conservatives—was the abolition of capital-gains taxes on firms selling their cross-holdings in other companies; this, it was hoped, would encourage Germany's corporate giants (which tend to own chunks of each other) to unbundle themselves. But then markets started to plummet, so the sell-off has been slower than expected.



One of the biggest strains on the welfare system is public pensions. On average, Germans retire at just over 60, earlier than people in most other rich countries, despite an official retirement age of 65. Pensions already swallow 12% of GDP. Compulsory pension contributions, paid half-and-half by employees and employers, have just been raised from 19.1% to 19.5% of gross wages.

But things are set to get a lot worse because the country is greying fast. Whereas currently there are two people of working age for every pensioner, on present trends there will be only one by 2035. Mr Schröder's government last year enacted a bill that encourages people to take out private pensions, helped by a government subsidy. Starting this year, they can put 1% of their pay into a private account, rising to 4% in 2008; but so far the take-up has been slow. That may be because, by most countries' standards, state pensions remain extremely generous. They now amount to 70% of the net average national wage, but this is set to fall to 67%, using a new system of calculation, which will be the equivalent of only 64% under the old system. Workers will also be held to contributing for 45 years to draw their pension in full. The current average is 37 years.

The costs of the health-care system, into which workers and employees jointly pay another 14% of gross wages, are also spiralling out of control. The Social Democrats say they do not want a two-tier system, as in America, but accept that change will have to come. That may take the form of providing all workers with free basic health care but perhaps charging for amenities that have hitherto been taken for granted, such as generous supplies of medicine and instant access to specialists.

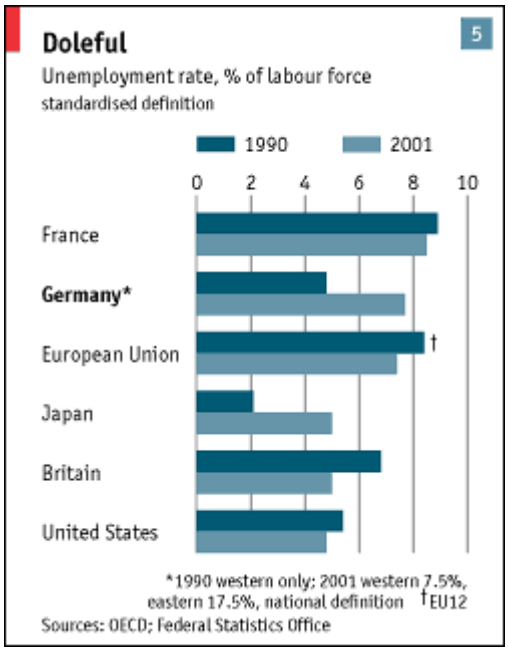
Unemployment benefit too is proving costly when so many people are out of a job. Benefits depend on age, length of previous service, family circumstances and so on, but at the top end of the scale a recipient with one child can get 67% of previous net income (up to a maximum of *euro*1,875 a month) for as long as 32 months. At the bottom end, a young jobless person who has never had a job or who has worked for less than two years is not entitled to any unemployment benefit at all—but may be eligible for (less generous) means-tested welfare assistance.

The biggest need of all, though, is to reduce unemployment itself, currently stuck at 9.8% by the

Germans' own seasonally adjusted measure (or 8.3% according to EU statistics). That means at least 4.1m workers without jobs. The most vital need is to free up the labour market, in particular by making hiring and firing easier and by letting labour become cheaper. In some respects, Mr Schröder's government has actually made matters worse in the past four years. For instance, it abolished the special status of low-paid workers in “DM630 jobs” (now known as *euro*325 jobs in the new currency), after the top limit on monthly earnings under this rule. Until then, employers had to pay only a modest flat-rate tax on such jobs, and employees nothing at all. They still escape, but employers now have to pay 22% in social-welfare contributions. The government also lowered the number of employees above which a company is obliged to have a works council and give workers time off for its business.

There had been hopes that Mr Schröder would continue with the liberalisation of Germany's restrictive shopping hours embarked on in 1996, but opposition from trade unions, as well as churches, proved too strong. Since the reform six years ago shops have been able to stay open until 8pm on weekdays and 4pm on Saturdays, but still not on Sundays, with only a few exceptions. If the rules were relaxed further, the sector could offer many more job opportunities (although small shopkeepers are strongly opposed to more liberal opening hours).

The main hope for at least starting to reform Germany's labour-cum-welfare system rests with the proposals to improve the labour market made by Peter Hartz, a top VW manager. When these were published in August, Mr Schröder instantly promised to implement them in full. If so, Mr Hartz claimed, his measures would create 2m jobs within three years. That may be too sanguine, but they would certainly make a difference.



Take Hartz

Mr Hartz's aim was not to change the labour market from the ground up—that, he said, was not his brief—but to make job placement more efficient, as well as to encourage temporary and short-term work, which Germany's highly regulated system currently discourages. The trade unions, which in the past have been fierce defenders of the status quo, have broadly endorsed the Hartz proposals “in principle”.

The most controversial proposal is the creation of “personnel service agencies”, to be run mostly by private temp agencies, which will take on people who have previously been unemployed and hire them out as temporary workers. Those who reject an offer of employment from such an agency will risk having their benefits docked.

Mr Hartz also tries to tackle the bottom end of the labour market to counter widespread tax evasion and create more legal jobs. One of his suggestions is for “mini-jobs” with private households, where people earning up to *euro*500 a month will pay no tax or social-security contributions and the employers will make a flat-rate contribution of only 10%, an improvement on the old “DM630 jobs”. Another is to give self-employed people tax incentives to set up companies (with a minimum of paperwork) known as “Me plc”, which allow them to earn up to *euro*25,000 taxed at a nominal rate of 10%, at the same time as collecting a state allowance that will gradually taper off over three years. Mr Hartz also wants to trim benefits for single people who refuse to accept a job simply because it would mean moving house.

In general, his proposals put more of an onus on the job-seeker to explain why a job is unsuitable before the state will provide him with welfare. All this will require a big change in expectations. The Hartz proposals would be an excellent first step towards labour-market reform, but some powerful trade unionists are beginning to grumble about the bolder of them. Depressingly, in recent weeks Mr Schröder has started to back away from his promise to adopt the lot, and started to water some of them down.

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Is the sun rising in the east at last?

Dec 5th 2002
From The Economist print edition

The mood in the "new states" is beginning to brighten

THE figures still look dismal. More than a fifth of the east German labour force is out of work, if you include those on the government's short-term job-creation schemes. Average wages are still only 77% of west German levels. Life in much of the "new *Länder*", as the former communist east is known, remains glum. The brightest and best of eastern youngsters still tend to head west. The downturn in the world economy has battered many new eastern companies. More recently, even nature has been hostile: the floods along the Elbe river in August wrought damage now put at *euro*9.2 billion, most of it in Saxony.

Even so, prospects in the east are, on balance, distinctly more hopeful than they were. Some parts of the region have started to exude a new sense of purpose, confidence and creativity. Manufacturing output has shot up. Clusters of automotive, electronic and high-tech industry are beginning to form, especially in Thuringia and Saxony, which were hubs of German industry before the second world war.

2001	Population m	GDP per person '000
Germany (total)	82.4	25.1
Western*	65.3	27.0
Eastern*	13.7	16.5

*Excluding Berlin
Source: Arbeitskreis Volkswirtschaftliche Gesamtrechnung

Bernhard Vogel, the Christian Democratic premier of Thuringia, says that it no longer makes sense to talk about eastern as opposed to western states. He points out that his capital, Erfurt, is actually further west than Munich, its Bavarian counterpart. Saxons and Thuringians are beginning to promote themselves as "Middle Germans"—as distinct from their poorer compatriots from Mecklenburg-West Pomerania and Brandenburg, the *Land* that surrounds Berlin.

Yet despite the vast dollops of cash and subsidies that have flown east, progress is slow. Since the end in 1995 of the construction-driven boom that followed unification, the area's economy has grown at about half the (already snail-like) pace of Germany's western states. Last year the eastern economy shrank, and this year it probably stood still.

Yet huge amounts of money continue to flow east. By the end of this year the tally of net transfers since unification will have reached about *euro*800 billion, nearly twice this year's budget for the whole of Germany. Last year the east received net transfers of *euro*75 billion. And Mr Schröder has agreed to a final "solidarity package", mainly to boost infrastructure investment, that will be dispensed from 2005 until 2019, worth a total of *euro*156 billion. All this is courtesy of German taxpayers, eastern as well as western, though the westerners, being richer and much more numerous, are stumping up the vast majority of it.

Buds of hope

It would be an exaggeration to say that the east now presents the "blooming landscapes" which Helmut Kohl, the chancellor at the time of unification, unwisely predicted in the first rush of euphoria; but progress has been immense. By virtually every material yardstick, life has improved. Rivers and air are incomparably cleaner. More than 800,000 new houses have been built since 1993, and the old central squares of just about every eastern town have been fastidiously restored. The new telephone system is

as good as any in Europe. New motorways link up every corner of the region. Even the poorest and most isolated little towns have shops stocked with a range of foods that would have been unimaginable in communist times. Car ownership has nearly trebled since 1989, and the wheezing old Trabant, old East Germany's family car for which eager buyers had to wait an average of nine years, is now a museum-piece.

Wages have nearly doubled in real terms since unification, GDP per head is up by 62% and pensions have soared—but there has been little or no growth in any of these since 1997. Labour productivity, by some calculations, has risen from 57% of western Germany's figure to 78% today, and in some manufacturing sectors it is as high or higher. Since 1990, more than three-quarters of industrial plant has been replaced. Even the retired and jobless, distressing as their plight remains, are financially better off than in communist times.

For sure, many *Ossis* (easterners), especially older ones, have yet to recover from the trauma of unification; some never will. After all, in its immediate aftermath, 7.5m of the east's 10m workers lost their jobs as whole industries were shut down. The number of industrial workers has plummeted from 7m to 700,000. The size of the labour force has shrunk by a third. And the 16.4m people who were living in the east in 1989 have come down by 1.8m, many of whom are reckoned to have moved over to the western side.

All this still haunts many easterners. They do not enjoy being told that 8,000 people now produce the same amount of steel in the east as 86,000 did a decade ago, or that the 40,000 Saxons still working on the land now grow more farm produce than 200,000 did in 1990. Nearly all public-sector workers in the east, doing exactly the same work as their western compatriots, still get, on average, only 90% of the western rate—and have to work 90 minutes longer per week for it.

Even in firms such as VW, where thousands of *Ossis* would be delighted to get a job, rates of pay and conditions in east German plants differ sharply from those in the west. At VW's biggest German plant, in Wolfsburg, not far from the western city of Hanover, the average working week is now 31.5 hours. Many of the workers have a four-day week. In Dresden, in Saxony, the average is 38 hours, and a six-day week is quite common. Yet pay rates in the east are considerably lower. Five-sixths of eastern industrial firms, covering one-third of industrial workers there, have opted out of collective wage-bargaining. The Saxon minister for the economy, Martin Gillo, says that, because average productivity in the east is still well below western levels, even with its lower labour costs the east is still not fully competitive.

Saxon angles

It is bad luck on the northern half of the old German Democratic Republic that the best economic prospects are concentrated further south, on a 220km-long corridor running more or less along the A4 motorway from Erfurt to Leipzig and on via Zwickau and Chemnitz through to Dresden. This is where, under the so-called *Leuchtturmpolitik* (lighthouse policy), business and government promote investment in beacons of industry and research that might bolster the local *Mittelstand*.

It seems to be working, thanks partly to large federal subsidies for investment. The Saxons boast that theirs is the only state in Germany where three car makers have chosen to invest in new plants: BMW and Porsche near Leipzig, VW in Mosel, near Zwickau, and in Dresden. All three firms say they are happy with the results. All insist that the quality of their workers is as good as in their western plants.

In Dresden, it is hoped that a high-tech cluster will form around two firms that specialise in semiconductors: Infineon, a spin-off from Siemens, and AMD, an American outfit headquartered in California's Silicon Valley. The pair have recently set up a high-tech joint venture with another American firm, Du Pont. Mr Gillo used to run AMD in Dresden until he became Saxony's economics minister earlier this year. He was born in Leipzig but has spent a good chunk of his working life in Silicon Valley, and he is bubbling with eagerness to see Dresden take off as a high-tech centre. Some 500 small software companies, he says, have sprung up in the area in the past few years.

Dresden is a marvellous mixture of old and new. The old city centre is an architectural jewel. According to its liberal mayor, the city is already Germany's sixth most popular tourist destination. In 2005 the exquisite Frauenkirche, flattened by Allied bombers in February 1945 in a raid that killed 25,000, will reopen after a meticulous resurrection, virtually stone by stone: a fitting symbol of Dresden's rebirth after six decades of totalitarian blight.

Serene again, the Elbe at Dresden

A notable change over the past few years has been the growth of a fierce new sense of local pride. Kurt Biedenkopf, the Christian Democrat who was Saxony's premier for the first decade after unification, says regaining that pride is the Saxon people's greatest achievement. But elsewhere in the east, too, the sense of having been taken over and done down by the west is fading.

After unification, almost the entire old establishment of the German Democratic Republic was swept away. Nearly all managers in industry and most university professors were chucked out, as were any public-sector workers with links to the Stasi, East Germany's secret police. Easterners, it was felt, were on the scrapheap.

Ossis rule OK

No longer. Five years after Mr Biedenkopf, once the Christian Democrats' general secretary, took over the running of Saxony (a post to which he was twice handsomely re-elected), his entire government was still made up of westerners, bar one *Ossi*. Now the only *Wessis* in the Saxon government are his successor as premier, Georg Milbradt, and his economics minister, Mr Gillo—who left the east as a child.

Eastern politics are beginning to reflect that new confidence. In the early 1990s Christian Democrats had swept the board in the east, thanks largely to Mr Kohl's status as Germany's great unifier. They still run Saxony and Thuringia and now also, in coalition, Saxony-Anhalt. However, within a few years many easterners were voting for the comforting certainties promised by the Democratic Socialists, a repackaged version of the old communists. Strikingly, in September's general election the ex-communist vote dived, because easterners now feel less need for a home-based party to bolster their identity.

In turn, *Wessis*, especially younger ones, are finding it easier to get along with *Ossis*. The cultural and social gap that was so apparent ten years ago is narrowing. The most striking sign of this is the surge of young *Wessis* at eastern universities, where more than a quarter of students now hail from the west. To be sure, there are practical reasons: the cost of living is lower, eastern universities are easier to get into, the staff-to-student ratio is more favourable, and academic standards remain fairly high. But social reasons play a part too. “My son used to think *Ossis* were really weird,” says a western editor whose son has gone to university in Saxony. “But now he says they're more interesting.” Not that social divisions have suddenly gone. A writer in Hamburg says most middle-class *Wessi* parents would still sigh if their son introduced his bride-to-be as “Nina from [eastern] Magdeburg”.

The other remarkable thing about the east is the way nearly all the region's businessmen and politicians complain about the burden of regulation, inflexible labour laws, high wages and social costs—just like their colleagues in the west. “The new states just aren't strong enough to bear the financial and regulatory burdens of the west,” says Mr Biedenkopf, who can take much credit for luring western and especially high-tech business to Saxony.

Eastern leaders argue for more exemptions from onerous rules. But many *Ossi* workers, still egalitarian by instinct, fear that looser rules for business in the east might cause workers to be exploited. “We are all Germans now,” is a common cry. That was why it was agreed in principle that wages and social benefits, although slightly lower in the east to begin with, should gradually converge. Mr Schröder has recently confirmed that within a few years public-sector wages must catch up. Alas, the sooner they do, the worse for *Ossi* job-seekers.

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Borderline cases

Dec 5th 2002
From The Economist print edition

Saxon snapshots

DRIVE two hours south-east of Dresden, close to the forested frontier with the Czech Republic, and you come to a sad little frontier town called Grossschönau. This is where Konrad Havlat, 47, prototype of the dogged, courageous entrepreneur who remained self-employed under communism, has turned himself from a humble leather-cutter into an independent businessman whose firm turns over *euro*4m a year and employs 64 people. He now churns out a bewildering variety of steel parts. Next year he intends to open a plant with 130 workers in the nearby town of Zittau.

But life for his kind of small businessman is hard and risky. On occasion, he admits, the banks have had to be kind to him. New firms like his are highly vulnerable to Germany's economic ups and downs. Just like his counterparts in western Germany, he complains bitterly about the inflexibility of the labour laws. He notes that social-security costs are much lower just across the border, in Poland and the Czech Republic.

Labour flexibility is essential to his success, he says, particularly being able to get his employees to work longer hours to fulfil urgent orders. He seems acutely aware that they could earn twice as much if they found similar jobs in, say, Stuttgart. At least a quarter of the people of Grossschönau, which once supplied the Saxon royal family with towels, have taken off since unification, mostly to seek jobs in the west.

An hour's drive north along the Czech and then the Polish border (which both seem pretty porous) takes you to Görlitz, on the west bank of the River Neisse that marks the post-war boundary with Poland. This is one of the most beautiful small towns in Germany, with many superbly restored buildings and squares. But the mood is sad. The place has too few Havlats, perhaps. Even more than Grossschönau, it seems empty of children and young people. The go-ahead seem to have taken flight, and tourism alone cannot sustain the place.

But business may perk up when Poland joins the European Union in little more than a year's time. Many Poles already cross the river from their decrepit side of the town, Zgorzelec, as they call it. Some Germans, for their part, have leased land on the Polish side, and people from Görlitz drive over for cheaper petrol and cigarettes.

Drive another 50km to the north-west, and you are faced with the bleakest of these three Saxon snapshots. Hoyerswerda must be one of Germany's ugliest towns. At the end of the second world war, it had just 6,000 people. After the war, the communists decided to exploit a huge coalmine underneath it, swelling the population to 70,000—housed in block after block of hideous high-rise concrete hulks, utterly devoid of a sense of community.

Back in 1991, the town gained a grim national notoriety for nastiness when a gang of racist thugs besieged an immigrants' hostel. Since then, a third of the people have gone. The young are still going. Of those left behind, a quarter have no job, or much prospect of finding one. Plainly, parts of the east are still slowly dying on their feet.

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Testing, testing

Dec 5th 2002
From The Economist print edition

Germany is flexing its muscles abroad, but does not yet know how to use them

IT WOULD make a neat paradox to be able to say that as Germany's economy is weakening, the country is becoming more powerful in world affairs—thereby inverting the conventional wisdom that Germany since the second world war has been an economic giant but a political pygmy. But it would not be quite true. Germany's economy, as we have seen, is not what it was: the gap with France's and Britain's has been getting narrower. And the country is certainly shedding the guilty inhibitions that for half a century have dissuaded it from asserting its national interests. Yet it seems that Germany is not sure what those interests are or should be.

Part of the explanation may be the giddying pace of recent change. During the eight years after unification in 1990, when Mr Kohl was in power, things had begun to move fast. Mr Kohl thought he knew what was good for Germany: “A European Germany, not a German Europe.” Germany had to remain anchored firmly in the steadying waters of Europe.

AP

Schröder and Chirac try to mend fences

But in the past four years under Mr Schröder, the pace has accelerated even further. The shift of the capital from quiet Bonn to history-heavy Berlin, a window on the Slav world to the east, has been a potent symbol. Mr Schröder feels a lot less weighed down by his country's past, and wants Germany to pursue its own course, albeit in concert with other vessels. But he has also found himself on occasions unsure how or where to navigate.

Perhaps the most striking recent example of this new-found independence was the opportunistic way he milked the anti-war mood in his country for electoral advantage. His disparaging comments about President George Bush and his “adventurism” in contemplating a war with Iraq were offensive enough to the Americans, but the diplomatic damage was compounded when his then justice minister, Herta Däubler-Gmelin, apparently accused Mr Bush of plotting war to divert attention from problems at home, likening his tactics to Hitler's.

The American administration had not expected Mr Schröder to give it enthusiastic backing for its policy towards Iraq, but American diplomats say that Mr Schröder twice assured Mr Bush that he would not make a fuss about it. So the president, they say, felt betrayed as well as insulted.

Class of '68

In any event, Mr Schröder's démarche may point up a deeper change in German thinking about foreign affairs. His government is full of “68ers”, who were waving, or even using, their fists in the street protests in 1968, or who were sympathetic to the cause. Mr Schröder himself was head of the Social Democrats' youth wing when it still described itself as Marxist, and acted as a defence lawyer to a member of the terrorist Red Army Faction.

Among many 68ers, a visceral anti-Americanism persists. For this generation of Germans, as one writer puts it, “the two landmarks were Auschwitz and Vietnam.” Part of their revolt was against their parents' generation, for their failure to stand up to Hitler, for the complicity of many of them in his crimes, and for their silence after the war. But another part of it was against America's military might—and its readiness to use force if need be—in the cold war. Such distaste for American power, still lingering among Greens and in some quarters of the Social Democratic Party, makes them promote the new Europe as a counterweight to the United States and NATO.

But none of this should be exaggerated. Many 68ers, including Mr Schröder and his foreign minister, Mr Fischer (who did use his fists against policemen in 1973), have genuinely changed their spots. Mr Fischer has said he owes more to Bob Dylan than to Karl Marx. More seriously, in recent times, he has often insisted on the importance of keeping the Americans engaged, with NATO, in Europe. Indeed, he deserves particular credit for persuading many of his old comrades that American power, at least usually, is benevolent. Likewise, Otto Schily, the interior minister (another 68er, who co-founded the Greens before switching to the Social Democrats), has demonstrated plenty of transatlantic goodwill by forcing through rigorous new anti-terrorist laws in the past year.

Though the Americans will not quickly forgive Mr Schröder for his seeming disloyalty, it is in nobody's interest to let relations stay sour, so the chances are that they will gradually sweeten over the next year or so, especially if American policy towards Iraq produces good results. The United States still has about 88,500 soldiers and airmen deployed in two main bases in Germany. If the servicemen or the bases were needed during hostilities with Iraq, it would be surprising if Mr Schröder did not let the Americans use them. The cornerstone of Germany's security is still NATO, though it may get harder to keep it in sound order.

A much more profound change has been the virtual breakdown of the Franco-German political alliance, the most important on the continent since the second world war. For sure, even in Mr Kohl's latter days the relationship was sometimes tense. But over the past decade circumstances have changed so utterly that the famous Franco-German “engine of Europe” will never be the same again, despite efforts in the past month or two to revive it. With Germany now so much larger, and the prospect that ten more countries will join the European club in the next year or so, France can no longer lead a diffident Germany to suit its own purposes.

The EU's eastbound enlargement, a project scarcely loved by France, is continuing the shift in Germany's, and Europe's, centre of gravity that started with the widening of NATO to take in Poland, the Czech Republic and Hungary. A further expansion of NATO, to include Balts, Slovaks, Slovenians and others, will alter Europe's shape still more. And even though Mr Schröder recently gave in—again, with astonishing opportunism—to the pleas of France's president, Jacques Chirac, that French farmers should continue to receive fat handouts, the day will come when farm subsidies will start to dry up. In sum, Europe is not going France's way, and Germany does not pretend that the Union is essentially a Franco-German enterprise any more.

But what, in German eyes, is it becoming instead? A few years ago, Mr Schröder was wooing Britain. Both countries' governments were touting a “third” or “middle” way. Britain's prime minister, Tony Blair, extolled the EU as a laboratory for free-market enterprise and liberalisation while also sounding politely sympathetic to Germany's wish for Europeans gradually to integrate. A year or so later, German-British friendship is not quite so intense. So long as Britain both stays outside the euro currency zone and fails to sign up fully to the Schengen pact that allows people borderless passage in most of western Europe, the Germans will never achieve the sort of intimacy with their neighbour across the Channel that they once enjoyed with France. So Mr Schröder's Germany is more independent—and less closely tied to old or new friends.

Made in Germany

What sort of Europe does Mr Schröder want for Germany? His most immediate worry is the stability and growth pact to which the 12 countries that have jointly adopted a common European currency are pledged. Ironically, it was the Germans who were chiefly responsible for creating the pact, to ensure that profligate euro aspirants, such as Italy, would be unable to run large deficits. Now the pact's conditions are causing particular hardship for the German economy, which needs anything but fiscal tightening. The French, for their part, are getting round the problem by blithely ignoring the pact.

A much bigger conundrum for Germany, however, is to find a new way for an expanding European Union to function. For all Mr Schröder's talk of asserting national interests, he and most Germans in what they like to call “the political class” are still accustomed to promoting German interests through the filter of the EU. Mr Fischer, who has proved a highly creative foreign minister, set the tone in May 2000 when he outlined his vision for Europe: a federal government of European states. Since then Mr Schröder has echoed the idea, albeit in more cautious terms, and so have other politicians of all stripes.

Europe, they insist, needs a stronger parliament of its own and an elected president of the commission. But they have no objection to a stronger Council of Ministers, as France and Britain want. Indeed, Mr

Schröder has suggested turning the council into an upper chamber of the European parliament, along the lines of Germany's own Bundesrat where the 16 *Länder* are represented. Compared with the French and British, the Germans remain fervent advocates of ever closer integration. They see the euro as paving the way for a tighter political union.

What about “enhanced co-operation”, the old jargon for a core group within the EU to keep things moving forward if sceptics such as Britain and the Nordics prefer to stay aloof? The French sometimes toy with the idea of setting up a *directoire* of top countries to run the show. But the Germans know that this would cause outrage among small countries and newcomers.

Mr Schröder is not, in fact, very interested in dreaming up foreign-policy visions for Europe. But he does have a strong sense that Germany should seek “normality” in the world, on the understanding that, although the crimes of the Third Reich must not be forgotten, modern Germans should now have, in his words, “the self-confidence of a nation that has come of age, that feels neither superior nor inferior to others.”

Hence his courageous decision that, if his country was going to be normal, it had to be ready to send troops abroad, if necessary to kill or be killed. His most creditable foreign feat was to send German forces to Kosovo in 1999, to help keep the peace in Macedonia a year later, and then, a year ago, to persuade the many doubters on his own side that he was right to send troops to Afghanistan. With 10,000 men abroad, Germany is now second only to the United States in the number of its troops deployed on such missions around the world. Germany's long-time foreign minister under Mr Kohl, Hans-Dietrich Genscher, once said that no German soldier would ever be sent to a country that had been conquered by the Germans in the second world war. In the Balkans Mr Schröder bravely broke that taboo.

Who will run the show?

The grandiose talk about the EU's new foreign policy continues to look silly whenever a real global crisis erupts, as it has done over Iraq. At such moments, the two countries in Europe that have kept a strong military tradition and serious fighting forces to go with it, France and Britain, invariably go their own way. These days that makes Germany feel all the more left out, particularly since the joint French-British declaration in St Malo in 1999 to create the embryo of a European defence policy together. “It is no good our pontificating from the sidelines,” says Christoph Bertram, a defence expert in Berlin. “After St Malo it was clear we had to get on board.”

Must they? Only up to a point. A readiness to send combat troops abroad (provided Germany is part of a collective effort) is new and, after early ructions on the left, has now ceased to be controversial. But, as American defence pundits put it, Germany has “no real teeth and a very long tail”. Despite its army of 310,000 (including 118,000 conscripts), the largest in Western Europe, it has a feeble fighting capacity. Its defence budget, at 1.5% of GDP, is among the lowest in the EU—although the revised budget figures for next year, which provide for an overall cut in government spending of 1.8%, show a 3.2% increase in spending on defence.

National pride, let alone nationalism, is still a delicate subject in Germany, certainly among the older generation. Only last year, a Christian Democrat leader got into hot water for declaring that he was “proud to be German”. Germany's president, Johannes Rau, a Social Democrat, was at pains to disagree: he was “glad” he was German, even “grateful” for being one, but he could not be proud of something he had not achieved himself. Mr Schröder said he was proud of what “people have achieved, and of our democratic culture”. One ex-68er, now a successful journalist, explains that even cheering on his country at international football matches still makes him feel awkward.

In most German eyes, it is still unacceptable to be rude about Israel's government, or even about individual Jews, though Israel's current leader, Ariel Sharon, may be an exception. In any other European country, the outspokenness on the Middle East of the Free Democrats' Mr Möllemann would not have caused a national row; nor would there have been outrage over a novel by Martin Walser, who had portrayed a fictional Jewish literary critic (bearing a striking resemblance to a real one in Germany) so unsympathetically that the broadsheet *Frankfurter Allgemeine Zeitung* refused to publish excerpts as previously agreed.

And yet, under the veil of building European unity, a new assertive prickliness sometimes shows up. The new Germans, less weighed down by guilt, are ready to express their frustration at the reluctance of countries such as Britain, France and Spain to pool their sovereignty. To those not in favour of much

more European integration, German talk of its “inevitability” can sound rather menacing.

At the same time, Mr Schröder is much more forthright than Mr Kohl used to be in telling the European Commission in Brussels to get off Germany's back. He is particularly protective about the rights of the *Länder*—for instance, to subsidise their local banks and ailing industries, even if that flouts European competition rules. And he is much more prepared to voice German resentment of the disproportionate sums his country still pays into the EU kitty.

All this seems reassuringly normal. After all, it is what other EU members, such as France and Britain, have been doing all along. Mr Schröder has moved Germany a long way towards freeing itself from the inhibitions of the past. But it will be a great deal longer before the shadows of history stop haunting the country altogether.

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Who's a German, then?

Dec 5th 2002
From The Economist print edition

Multiculturalism still jangles national nerves

KATS

Side by side doesn't mean together

IT IS an oddity of modern Germany that, even though the country has been friendlier than any other in Europe to asylum-seekers and refugees, foreigners settling there have found it extraordinarily hard to become German. There are 7.3m residents who do not have German citizenship, nearly 9% of the population. Some demographers argue that Germany will need 260,000 immigrants a year for the next 20 years just to keep its present population stable and avoid a financial crisis in its welfare and pension systems. Yet few indigenous Germans accept the notion that Germany is, or should be, a multicultural country.

Mr Schröder, to his credit, has started to change this by updating the rules on naturalisation, which were based on an imperial law of 1913 that defined Germanness mainly by blood. This meant that descendants of Germans who had settled in Russia under Catherine the Great could become German again at the stroke of a pen without knowing a word of German. Since the Soviet Union broke up, more than 3m have done so.

For the 2.5m German residents of Turkish origin (of whom about 500,000 may now have got citizenship), many of them second- or even third-generation, it has been much harder to get German passports. But now, thanks to Mr Schröder's change in the law, children of foreigners born in Germany, provided at least one parent has lived there for a minimum of eight years, are automatically given German citizenship at birth—though they have to choose whether to keep it when they come of age.

Earlier this year, Mr Schröder passed a law which marked Germany's first serious effort to match immigration with Germany's economic needs, with provision for a points system to lure skilled workers from abroad. The law, due to come into force next year unless the Constitutional Court blocks it, builds on a controversial scheme endorsed by Mr Schröder two years ago to give permits to up to 20,000 computer specialists from India and Central Europe to work in Germany on five-year contracts. The new bill also makes it easier for foreign students educated at universities in Germany to stay on, and easier for self-employed foreigners to work in Germany.

Many politicians, mostly on the right, have opposed the changes. Two years ago Jürgen Rüttgers, the Christian Democrats' leader in North Rhine-Westphalia, Germany's most populous *Land*, demanded "*Kinder statt Inder* (children, not Indians)", meaning that Germans should have more babies instead of relying on workers from abroad. Mr Stoiber backed him, suggesting that the current rate of child benefit should be tripled. Friedrich Merz, the Christian Democrats' then leader in the Bundestag, said immigrants must accept that each country has its *Leitkultur*, or predominant culture, to which newcomers must adapt. That set alarm bells ringing in Germany.

By any standard, Germans of foreign origin—and particularly from Turkey, easily the biggest minority—are woefully under-represented in politics and public life. For example, only a couple of them sit in parliament, compared with 38 non-whites currently in Britain's two chambers. Being generous to asylum-seekers is one thing, but absorbing foreigners into the German family still revives old neuroses about national identity.

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The trouble with contentment

Dec 5th 2002
From The Economist print edition

When life is so pleasant, there is little incentive for radical change

KATS

If only they could be bold about everything

IT WOULD be entirely misleading to paint Germany as a country that is shabby or miserable, prone to political instability or in danger of terminal economic decline. On the contrary, it remains rich, stable and, for the overwhelming majority of its people, very pleasant to live in. Growth may be slow, unemployment high and the *Mittelstand* gloomy, but on the whole the climate of society still strikes the outsider as fairly sunny. There is hardly any visible poverty of the kind found in the more depressing bits of Britain or France. Germany's high-tax regime and rigid labour markets may be damaging to its economic prospects, but its welfare and health-care systems are generous and its infrastructure is superb.

Nor is the pleasantness of German life just about material living standards. Modern architecture, on the whole, is refreshingly enterprising. Many companies and institutions take pride in enlivening their physical surroundings, commissioning public works of art, such as sculptures and fountains, for all to enjoy. There is also a strong awareness of environmental issues, so recycling is taken to heart and bicycle paths and forest trails are abundant.

One of Germany's greatest attractions is its regional variety, which goes a long way towards giving Germans a sense of local community and pride. Berlin may, since resuming its role as capital, have become *primus inter pares* in a way that Bonn could never have been, but half a dozen other cities can lay claim to excellence in their particular fields, and gather up some of the country's brightest and best. Hamburg still has the pick of the media, Frankfurt has the finance, Munich has an enviable mix of business, media and culture (“laptops and *Lederhosen*”). The Constitutional Court is in Karlsruhe; the headquarters of the country's vast labour office is in Nuremberg; the biggest art market is in Cologne; the main trade union federation has only fairly recently moved from Düsseldorf to Berlin.

This decentralisation is good for politics. Most of Germany's top politicians (including Messrs Schröder, Stoiber and Kohl, among many others) first made their mark in one of the 16 *Länder*, which each has its own parliament and government. Each *Land*'s ruling party (or parties, if there is a coalition) sends representatives to the Bundesrat, Germany's federal upper house, which can block about half of all legislation, particularly the financial sort. The *Länder* have no power to raise taxes, but merely distribute cash from budgets set at federal level. However, they control education, the police and prisons, and can affect business by touting for investment, lobbying in Berlin and Brussels, and helping to speed up planning permission and cut through red tape.

Germany's post-war decentralisation (as well as an electoral system based on proportional representation) was, in fact, decreed by the conquering Allies to ensure that power could never again be monopolised by one man at the top. But whatever its origins, it has suited the country very well—and helps to explain why, to a German, federalism means something much more positive than it does, say, to a Briton.

But decentralisation has drawbacks too. For one thing, because decisions are taken on several levels, rapid or drastic change is hard to achieve. It feeds a tradition of compromise and consensus to which most German politicians are firmly wedded. And it makes governments more reluctant to contemplate big changes when they are needed.

Don't wait too long

The question is, does Mr Schröder believe that fundamental changes are needed? Or does he hope that, as the world economy recovers and Germany's eastern states become more self-sustaining, things will gradually come right anyway? The answer is probably a bit of both. Mr Schröder is an intelligent man who listens to a lot of people, including many of Germany's big businessmen. Even since the election he has acknowledged that his government must trim welfare and health-care costs and do something to lighten the pensions burden. But he himself, brought up in poverty by his mother, who worked as a charwoman to keep them going (his father having been killed in the war), is a product of a system that he admires; after all, it served Germany handsomely in the years of reconstruction, and made it the rich and steady country it still remains.

Much depends on what happens in the next four years. It is conceivable that if the economic situation gets much worse, the chancellor might steel himself for a break with the consensual past, even at the risk of labour strife. Some say that only a government of the centre-left has a chance of persuading the unions to accept an end to the job-destroying status quo. Others argue that the only way to save Germany from permanent stagnation is a “grand coalition” of the two main parties, which could muster an enormous majority to force through unpopular decisions. But a period of grand coalition in the 1960s is still remembered for producing more problems than solutions.

Commentators, especially from abroad, have been predicting gloom and doom for Germany's economy for a decade or two. It still hasn't arrived. But growth has clearly slowed down dramatically, and governments at the federal, regional and local level have started running out of cash. So far, for the large majority of Germans in work and even for the 4m without it, the slow decline is unlikely to mean empty wallets, let alone empty stomachs. This is not like the 1920s and 1930s, when the jobless were truly desperate and therefore easily drawn into the web of totalitarian politics. But someone—perhaps the chancellor after Mr Schröder, or the one after that—needs to start making radical changes. Otherwise, a few years hence, life in Germany really will become a lot less pleasant.

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Dec 5th 2002
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The author would like to thank many people across Germany for their advice and kindness in taking the trouble to discuss their country so frankly. None of them bears responsibility for any mistakes or misjudgments in this survey.

Among the many people, organisations and companies that helped the author are:

Dr Andreas Busch of the Centre for European Politics, Economics and Society, University of Oxford; Ambassador Leopold Bill von Bredow, Dr Martin Koopmann and Dr Angelika Volle at the German Council on Foreign Relations, Berlin; Professor Lord Dahrendorf; The Konrad Adenauer Stiftung; Katrin Bether and Dr Katharina Schöps of the RKW Sachsen management consultancy; Gabor Steingart and Joachim Preuss at *Der Spiegel*; Peter Senft at IG Metall in Berlin; Hanns-Eberhard Schleyer of the Zentralverband des Deutschen Handwerks in Berlin and his press officer, Alexander Legowski; Manfred Güllner of the Forsa polling agency; Ashley Carmody at the Allensbach Institute; Prof Dr Klaus Zimmermann of the Deutsche Institut für Wirtschaftsforschung; Lutz Raetig of Morgan Stanley; The Bundesverband der Deutschen Industrie; The Dachorganisation der Gewerkschaften in Deutschland; Claus Strunz, editor-in-chief, *Bild am Sonntag*; Professor Barbara John of the Beauftragte für Migration und Integration des Senats von Berlin; Dr Günter Rexrodt of the Free Democratic Party; Christoph Keese, Wolfgang Münchau and Thomas Hanke of *FT Deutschland*; Cem Özdemir of the Green Party; Dr Alfred Tacke, state secretary, Ministry of Economics; Daniel John Nicolai of the English Theatre, Frankfurt; Stefan Schulte of VW in Dresden and Dr Christoph Bertram of the Stiftung Wissenschaft und Politik in Berlin; Dr Josef Joffe, editor of *Die Zeit*; Walter Allwicher of the Deutsche Börse in Frankfurt; Dr Ralph Solveen of Commerzbank in Frankfurt; Dr Hans Tümmers and Dr Keith Goffin of the Stuttgart Institute of Management and Technology; Andreas Richter of Stuttgart's chamber of commerce and industry; Professor Dr Lothar Späth, chairman of Jenoptik; Dr Wilfried Prewo of the chamber of commerce and industry in Hanover; and Prince and Princess Michael and Philippa Salm-Salm of Wallhausen.

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Dec 5th 2002
From The Economist print edition

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Advertising

High hopes in adland

Dec 5th 2002
From The Economist print edition

The advertising industry is at long last showing definite signs of life. But the outlook remains challenging

AFTER the worst slump in advertising since the Great Depression, suddenly talk of recovery is in the air. In America, the big broadcasters are celebrating a rebound in commercials on network television. News Corporation's first-quarter profits more than doubled: a “resurgence of the advertising market,” said its boss, Rupert Murdoch. He is not alone. Across the board in America and Britain, media-buying firms, TV broadcasters and radio and billboard companies have been making positive noises about the future. Even print advertising looks better. The December 2nd issues of several American magazines were heavier—with ad pages 70% up on a year ago in *Newsweek*, 27% in *Time* and 13% in *BusinessWeek*.

After an awful start to the year, most forecasters of ad spending are predicting a better end, a gradual improvement in 2003 and a return to normal (ie, pre-tech-bubble) levels in 2004. On December 3rd UBS Warburg said it now expects global ad spending this year to be 1.1% lower than in 2001. It predicts growth of 2.6% next year, followed by a livelier 5.3% increase in 2004. It expects America to lead a “soup-dish” recovery—long and shallow—until the presidential elections and Athens Olympics pump up the market in 2004.

Much of the optimism in adland is down to one thing: buoyant American network-TV ad revenues. But the reason for that is partly artificial—a freak shortage of ad space in both the upfront (futures) and scatter (spot) TV markets in America. After a year of bargains in 2001, advertisers hedging against rising prices for TV space in 2002-03 rushed into the market early. A startling 80% of space for shows airing from now until May is already sold. That, plus car promotions and mid-term election spending, dramatically cut inventory, forcing up prices for airtime by a hefty 70%. Forecasters expect the shortage to boost radio and print prices as advertisers seek other, cheaper places to sell.

Notable bright spots include advertising by the entertainment industry to promote DVD sales, which are booming and often generate bigger profits than box-office receipts. Mike Dunn at Fox Entertainment raves that DVDs have “changed the economics of the film industry”. Car makers, drug firms and packaged-goods groups also plan to keep advertising heavily.

But enough risks remain that few in advertising can feel confident enough even to dream of partying once again. Advertising traditionally tracks global GDP. Prospects for growth are terrible in Germany and weak in France and in Japan: big ad markets all. Although the American consumer now looks a little less ready to crumble than a month ago, that remains a real danger—even without a war with Iraq. A

reluctant American consumer would devastate the ad industry. Like many in the industry, Sir Martin Sorrell, boss of WPP, the world's biggest advertising firm, fears a consumer-led double-dip recession.

However the economic cycle turns, the advertising industry faces a long period of structural change, from which the winners are as yet hard to predict. This change has gathered pace over the past five years, but was somewhat obscured first by the boom, then by the cyclical bust.

The medium is the message

Newspapers and magazines face an uncertain future, though how uncertain varies by category. Business titles have been hit by the collapse in financial advertising, but that should rebound as investment banking (eventually) starts to recover. Health titles catering to the ageing “silver” market should remain robust. But the proliferation of print titles (more than 500 launched in America last year) and competition from new media such as the Internet will ensure tough times for the crowded middle market. At a recent conference in Phoenix, Time Inc, Hearst and Reader's Digest all gave warning that, unless subscription rates rise, profits will dwindle as readers decline and ad sales fall. “We have no choice but to change”, said Thomas Ryder, head of the Reader's Digest Association.

Ironically, given its contribution to the present bout of optimism, TV advertising also faces serious long-run threats—from ad-evading systems such as TiVo to the proliferation of other media—which the industry may be inadvertently assisting. Sir Martin argues that by raising prices above inflation, even as audiences decline, TV owners have driven advertisers into the arms of new sorts of media. “There has been a shift from network TV. Real long-term growth may not return.”

There is a sense of panic in adland, reflected in a plethora of new marketing books with hair-raising titles, such as “The End of Advertising as We Know It”. As better manufacturing raises quality, more products are becoming commodities, while tougher competition and the growth of private labels are leading to shorter shelf lives for even the most innovative goods. Differentiating one product from another is harder—and advertisers need to find ever more creative ways to do it. That will probably mean more marketing not less, but once-neglected (and cheaper) methods of selling—direct, outdoor, guerrilla marketing, sponsorships and product placements—may triumph over traditional print and TV ads. The new James Bond film, “Die Another Day”, has taken product placement to a whole new level, promoting everything from Heineken beer to Omega watches and (invisible) Aston Martin cars. Coca-Cola sponsored Fox TV's “American Idol” show. BMW cars are starring in Internet mini-movies.

The ad agencies, too, face pressure to change. In the 1990s, thanks to Sir Martin, they went on a buying frenzy, using their high share prices to add a host of “below-the-line” services, such as public relations, brand consulting, Internet advertising and market research. Troubled Interpublic, one of the big three agencies, must rue its indifference to quality or price.

Morphing from peddlers of creative TV ads into marketing-services firms has boosted margins and revenues, says Lorna Tilbian, an analyst at Numis Securities. “The more media fragmentation advertisers face, the more they need full-service agencies to target the customer,” she says. But the shift from TV and print has not made agencies any less vulnerable to the cycle: public relations has suffered more even than advertising in the downturn.

Nor has integrating new businesses typically delivered all the promised structural efficiencies. Omnicom, another of the big three, managed integration well. Interpublic's spending spree, by contrast, ended in a huge accounting scandal. Lack of effective integration, particularly at the top, has allowed naughty practices to flourish, such as over-billing clients, which are only now coming to light.

And just as the opportunities to grow through acquisition are drying up, agencies face price deflation, says Matthew Owen of Morgan Stanley. As agencies scale up to become one-stop global marketing shops, clients are squeezing them harder on price. If service-price deflation takes hold, the agencies may not see profits rebound much even during the long-awaited upturn. Nobody in adland should crack open the bubbly just yet.

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Right-wing media

It pays to be right

Dec 5th 2002
From The Economist print edition

There are profits in conservatism

WHEN Al Gore complained last week about the right-wing bias of the American media, in an interview with the *New York Observer*, it was but the latest contribution to a growing fuss. “The media is kind of weird these days on politics,” grumbled Mr Gore, “and there are some major institutional voices that are, truthfully speaking, part and parcel of the Republican Party.” Top of his list of offenders, which included the *Washington Times* and Rush Limbaugh, was the Fox News Channel. It was the revelation in Bob Woodward's new book, “Bush at War”, that Roger Ailes, head of Fox News, advised George Bush after September 11th that kicked up the stink in the first place.

It would be strange if politicians did not whinge about partisanship in the media. The oddity that this latest fuss exposes is the amazing durability in America of the myth of media impartiality. There has been an outpouring this year on the subject—though most, such as Bernard Goldberg's “Bias: A CBS Insider Exposes How the Media Distort the News”, lament the “liberal bias” in America's media.

Fox News, part of Rupert Murdoch's News Corporation that consistently beats CNN in the ratings, is now the liberals' pet villain. Its success reflects a business as much as a political strategy. With the proliferation of cable-news channels—CNN, MSNBC, Fox News, CNBC, Bloomberg—the market in America has become more segmented. Mr Murdoch spied a niche for a snappier, noisier form of in-your-face TV news that would outshine the increasingly staid formats used by CNN—and serve viewers fed up with liberal leanings.

Gino Domenico

The lucrative Mr O'Reilly

Fox News insists that it is not biased towards the right, but rather making up for liberal bias elsewhere: its slogan is “We report. You decide”. But its most popular hosts, such as Bill O'Reilly, have made an art-form of the conservative political rant. The formula has been a huge commercial success. Operating profit at News Corporation's cable-network programming (which also includes other channels) more than tripled year-on-year in the quarter to September 2002, to $118m.

Mr Murdoch has pioneered the market in conservative political views, whether on Fox News or in newspapers, from the *New York Post* to the London *Times*—though even he is prevented by “impartiality” regulations from exporting the Fox News formula to Britain via his Sky News. But he is not alone in pursuing this booming market. Radio has long understood the pull of right-wing talk shows, led by Mr Limbaugh. Now publishers are at it too.

A rush of right-wing political books have stormed the bestseller lists. Some are from established conservative publishers, such as Regnery Publishing, which put out Mr Goldberg's tome. But mainstream publishers are now also after the profits in conservatism. Ann Coulter's “Slander: Liberal Lies about the American Right”, was published by Crown, part of Bertelsmann. And “Let Freedom Ring: Winning the War of Liberty over Liberalism”, by Sean Hannity, a Fox News talk-show host? Its publisher was none other than Mr Murdoch's HarperCollins. Now that's synergy.

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Digital copyright

Overkill

Dec 5th 2002
From The Economist print edition

A controversial law is put to the test

WHEN Dmitry Sklyarov, a young Russian computer scientist, got up to deliver a technical paper at a conference in Las Vegas last year, he little suspected that he was about to become something of a global celebrity. But soon after delivering the paper he was arrested by the FBI for breaching the Digital Millennium Copyright Act (DMCA), a 1998 American law that bans any efforts to bypass software that protects copyrighted digital files. The arrest sparked a rash of protests in both America and Europe. The Internet hummed with indignation. Charges against Mr Sklyarov have since been dropped, in exchange for a promise to testify. But the case against his employer, Moscow-based ElcomSoft, went ahead this week in San Jose, California.

The closely-watched trial is the first criminal prosecution brought under the DMCA, a law loathed by Internet enthusiasts. The trial will mark a crucial stage in the growing struggle between industries supplying content and those arguing that overly strict enforcement of copyright may crush the creativity of cyberspace.

ElcomSoft is being prosecuted for selling in America, over the Internet, a program developed by Mr Sklyarov, which allowed purchasers to bypass the copy-protection features of Adobe's popular e-book software. ElcomSoft, which sells various software utilities, says that it never intended to breach the law. It seems eager to fight the case. Mr Sklyarov is, in effect, testifying for both sides, and proceedings were delayed until special visas were obtained both for him and for Alex Katalov, ElcomSoft's chief executive, to attend the trial. The firm's lawyers have echoed the arguments of long-standing opponents of the DMCA. They claim that the law is so vague as to be unconstitutional, that it breaches the first-amendment free-speech rights of programmers, and that it brushes aside “fair use” rights of consumers protected by mainstream copyright law.

The DMCA makes it a criminal offence to circumvent in any way technology used by copyright holders to limit access to their work. It also outlaws the manufacture or distribution of any tools or technologies that make getting around such controls easier. Critics complain that this is overkill, criminalising much perfectly innocent research by computer programmers. Moreover, they say, even legitimate efforts to copy protected material, such as for quotation, criticism, or purely private use, are turned into crimes by the DMCA's sweeping provisions.

As a matter of fact, Adobe's software allows e-book publishers to set their own level of protection. Many publishers have chosen to allow users to make copies for private use on different computers, or for lending copies to friends. But if publishers opt for maximum protection, then e-book purchasers cannot do many of the things that are perfectly legal with printed books, such as copying sections.

So far, the federal judge conducting the trial has dismissed ElcomSoft's constitutional arguments as irrelevant to the criminal case. But these are likely to become the key issues if the case, or another DMCA test case like it, goes all the way to the Supreme Court. Given the vehement arguments made on both sides of the issue, it is not clear how the Supreme Court would rule. Meanwhile, content industries, led by the mighty American movie and music businesses, are squaring off against critics not just in the courts, but also in America's Congress, where bills both to soften the DMCA's provisions and to make them even more draconian have been introduced this year.

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Vodafone versus Vivendi

Clear as mud

Dec 5th 2002
From The Economist print edition

Vivendi has won control of Cegetel, but its long-term strategy is still murky

Get article background

WHAT is Jean-René Fourtou, boss of Vivendi Universal, up to? His struggling French conglomerate has been fighting Vodafone, the world's largest mobile operator, over Cegetel, France's second-largest telecoms company, in which both firms own stakes. Vodafone's strategy was clear. It wanted control of SFR, Cegetel's subsidiary and France's second-largest mobile-phone operator, to plug the last big hole in its European coverage "footprint".

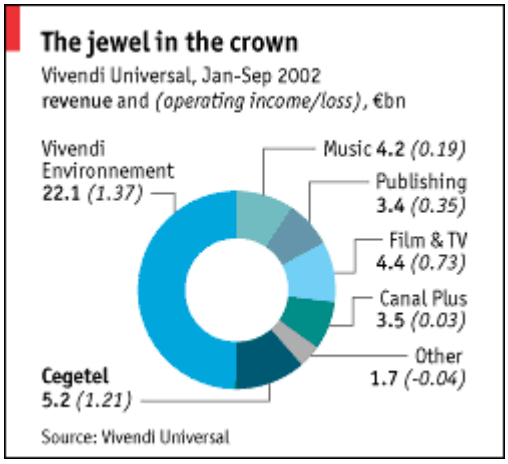
Why Vivendi was trying to stop it, however, is anybody's guess. In September, Mr Fourtou, who took charge in July, declared that "Vivendi Universal is basically an entertainment company". That signalled a retreat from the tarnished vision of his predecessor, Jean-Marie Messier, who had tried to turn a dull utility company into a media, telecoms and entertainment giant. As Vivendi began to unload assets to pay its *euro*19 billion ($19 billion) debt, selling its stake in Cegetel seemed logical. Vodafone duly offered to buy Vivendi's 44% holding for *euro*6.8 billion and the stakes held by British Telecom (BT) and SBC, an American regional operator, for a further *euro*6.3 billion. But Vivendi decided that it wanted to hold on to its stake after all and refused to sell.

At first, this simply looked like a ploy to get Vodafone to up its bid, which it declined to do. Vivendi then launched its own initiative to take control of Cegetel. Did this mean that Mr Fourtou had concluded that his plan to focus Vivendi purely on entertainment was a bad idea?

On December 3rd, Vivendi agreed to pay BT *euro*4 billion for its 26% stake in Cegetel, thus giving Vivendi a 70% stake and thwarting Vodafone's bid for control. Vodafone, which still plans to buy SBC's 15% stake for *euro*2.3 billion, will end up with just 30%. The company tried to put a brave face on this outcome, claiming in a statement that it was "a long-term investor in Cegetel and SFR" and that it "looks forward to continuing its successful partnership with Vivendi". Vodafone seems prepared to play a long game and is confident that it will ultimately win control of SFR.

But despite Mr Fourtou's triumph, his strategy remains as clear as mud. He has said, for example, that he thinks *euro*8.5 billion would be a fair price for Vivendi's original 44% stake in Cegetel. So he may still be holding out for a better offer. Vodafone has until December 10th to make a new bid, though it seems unlikely to do so.

It is also possible that Mr Fourtou wants Cegetel purely for short-term cashflow, as he decides what kind of company Vivendi should be. Cegetel generates a lot of cash and a disproportionate chunk of Vivendi's profits (see chart). By Mr Fourtou's own admission there is no synergy between Vivendi's entertainment and telecoms divisions, and one of them will have to go within the next couple of years. Having indicated in September that he wanted to focus on entertainment, he may now be reconsidering. But he seems in no hurry to decide. The cash from Cegetel gives him more room to manoeuvre, and means he can defer the decision.



Or perhaps he does have a grand new plan after all: to spin off Vivendi's American units—a movie studio, a record company and a collection of television assets—and scale back Vivendi to concentrate on telecoms and pay-TV in the French market. If so,

Cegetel could be central to the company's future. This week Mr Fourtou confirmed that he was considering a spin-off of Vivendi's American holdings. That would be consistent with the plan to refocus on the domestic market—but it would represent a reversal of his position.

It would also heighten tensions with Vodafone. In an interview with *Le Figaro*, Mr Fourtou claimed that telephony is “an essentially national activity” and that there were few benefits from operating in more than one country. Vodafone takes the opposite view: its international coverage gives it economies of scale in research and development and greater clout with equipment vendors.

As Vivendi's strategic paralysis continues the real winner may be Orange, France's leading mobile operator, and its debt-laden owner, France Telecom. (Orange's chief executive, Jean-François Pontal, was expected to announce his retirement this week.) The bickering over Cegetel may mean that SFR poses less of a competitive threat than it would with Vodafone's muscle fully behind it. And as the dysfunctional alliance between Vodafone and Vivendi limps along, French consumers, fewer of whom carry mobile phones than their British, German or Italian counterparts, will be the losers.

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Asbestos lawsuits

Light in the dust

Dec 5th 2002 | NEW YORK
From The Economist print edition

Solving the asbestos litigation mess

AMONG the unexpected stars of the recent stockmarket rally have been several firms in dull slow-growth businesses. These included Crown Cork & Seal (cans), Georgia Pacific (paper) and W.R. Grace (chemicals). The best explanation for their rise is a legal settlement confirmed on November 29th by another plodder, Sealed Air, best known for making bubble wrap. Sealed Air agreed to pay one-third of its then market value, about $730m, in cash and shares to a trust fund being created out of the bankruptcy of Grace to benefit asbestos victims. The deal could have huge implications for thousands of other firms facing asbestos litigation.

The travails of Sealed Air, which never produced, sold, marketed or even touched asbestos, had come to symbolise the toxicity of asbestos litigation, which through millions of lawsuits has led to the bankruptcy of more than 70 firms. The number of jobs lost due to these lawsuits may be as high as 60,000, according to a study by Joseph Stiglitz, a Nobel-prize-winning economist, on behalf of the American Insurance Association. Their total cost could reach $200 billion, he estimates.

Slowly, the litigation has spread from firms involved directly in the mining of asbestos or the manufacture of asbestos-based products to others that had only peripheral involvement. Crown Cork & Seal was overwhelmed by suits tied to a company it owned briefly in 1963, long before any health hazards were widely known. The litigation against Sealed Air was particularly jarring because it came by way of an acquisition structured to avoid precisely this problem. In 1998 the firm paid $5 billion for a division of Grace that made plastic shrink-wrap for meat and fish in grocery stores. The business had never used asbestos. Sealed Air took care to win from Grace an indemnity against any possible asbestos litigation.

But that guarantee in effect disappeared in April 2001 when Grace declared bankruptcy. A year later, lawyers for asbestos victims sued, arguing that Sealed Air's acquisition had been fraudulent and that Sealed Air had bought Grace's legal liabilities with its operations. In July Sealed Air's share price plunged from $40 to $14.

Until recently, the mood in the markets had become sceptical about the prospects of any firm with the slightest exposure to asbestos litigation reaching any solution short of bankruptcy. But out of the public eye lawyers in a handful of key cases began negotiating around a 1994 amendment to federal bankruptcy law that lets firms settle litigation by creating a trust fund for victims. The idea first emerged in the 1980s asbestos lawsuits against Manville, whereby the equity of the firm ended up owned by the trust for victims. In May, Pittsburgh Corning, a bankrupt building-products company, announced a deal that would include a trust to be funded, in part, by its half-owner, PPG. Then Babcock & Wilcox struck a similar deal, with a contribution to a trust fund provided by its parent, McDermott International.

All this failed to lift the stockmarket gloom over other asbestos-exposed firms, perhaps because they were small deals and because doubts remained about how much of a precedent they set for companies that had not (yet) gone bust. This has changed with the Sealed Air deal, which shows conclusively that a big firm contributing to a trust does not necessarily have to be in bankruptcy. There is optimism that similar arrangements can be made by ABB, a Swiss-Swedish giant, through a bankruptcy of its American subsidiary, Combustion Engineering, as well as by Honeywell and by Halliburton, which bought Dresser Industries in 1998 and found itself with a costly asbestos liability.

Any arrangement that lifts the asbestos cloud now hanging over many firms could have huge benefits for victims as well as firms. Within minutes of Sealed Air's announcement on November 29th its share price rose by 40%. That increased the value of the 9m shares to be put in the trust under the settlement by almost $100m.

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Movies in South Korea

Hello to arms

Dec 5th 2002 | SEOUL
From The Economist print edition

An industry that is literally booming

NORTH KOREA has been many things to the south: enemy, lost family, a worry for war-fearers. But not material for a popular movie. Not, that is, until “Shiri” invaded theatres in the south in 1999, becoming the most successful Korean film ever and winning export deals from Europe, America and Japan. A one-off, critics thought, until 2000, when “Joint Security Area” (JSA) broke Shiri's record. Now it seems that Korea's film industry is waking up—and that North Korea really sells. Both blockbusters treat inter-Korean relations positively, though both end tragically.

Indeed, South Korea's government now wants in on the opportunity. As the need to give vast amounts of land over to military purposes fades, why not let movie-making replace it? Last month, South Korea's defence ministry said it would allow use of its military grounds and weapons for film production.

AP

Don't shoot, we're actors

This is a big change, given that lack of co-operation by the army meant that the makers of “JSA” spent $1m on a replica of the Panmunjom truce village. Forthcoming attractions that will benefit from this military largesse include: “Flag High in the Air”, a love story set against the Korean War by the director of “Shiri”; “Blue”, a marine action film; “Blue Sky”, about friendship and challenges facing air-force pilots; and “Red”, a comic drama about North Korea. Really.

But access has strings attached. The government insists that films it supports should portray the South Korean armed forces favourably. It rejected “Waterfront”, a story about a crazy woman sexually violated by some marines, and “The Trigger”, a tale about a front-line guard who falls for a virgin female ghost.

The dozen or so North Korea-related pictures in the pipeline could make or break the booming film industry, which is gaining ground at home against foreign imports. It is on course to match last year's record market share of 46%, up from 33% in 2000.

But like other movie-makers, Korea's seem prone to the industry's usual vices, including out-of-control budgets for production and marketing, and waning creativity. The dream of becoming Asia's Hollywood will depend crucially on cracking foreign markets, through exports and above all remakes. Anybody for Ben Affleck and Jennifer Lopez in a Hollywood remake of “The Trigger”?

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Fast food in America

Not so fast

Dec 5th 2002
From The Economist print edition

An industry suffering from indigestion

SINCE Jazlyn Bradley, a 19-year-old teenager from the Bronx weighing 122kg (268lbs), sued McDonald's last month for making her fat, the prospect of a mountain of obesity lawsuits has frightened America's fast-food industry. But a bigger short-term threat for peddlers of hamburgers, pizzas and fried chicken comes from customers still watching their waist-lines.

Same-store sales at fast-food chains such as McDonald's and Burger King are declining, and a new business dubbed “fast casual” has sprung up. Comprising gourmet sandwich, salad and soup chains, Mexican outlets and traditional American diners, fast casual offers healthier menus, higher-quality, fresher, more varied food and a more tempting ambience than plastic chairs and garish lighting. With sales of $5 billion a year, fast casual is tiny compared with the $153 billion fast-food market, but it is growing by 12% a year.

The most successful brands include Schlotzky's, with 650 restaurants in 38 states and ten foreign countries. It specialises in exotic sandwiches such as the “Asian almond chicken wrap”, trumpeting seven grams of fat or less. Panera Bread, with 414 outlets, serves deli-style sandwiches and soups, and boasts soaring profits. Cosi coffee and deli bars sell built-to-order sandwiches. In-N-Out Burger has over 140 outlets in south-west America promising fresh beef, hand-leafed lettuce and no heat lamps to revive soggy burgers.

The loss of upmarket consumers to fast-casual rivals is hitting McDonald's and others at a time when mainstream customers, the delightfully labelled Hoo-Foos—Heavy Fast-Food Users, also known as young, single males—are being disproportionately hurt by unemployment and falling incomes. McDonald's, the biggest chain, with 13% of the fast-food market compared with Burger King's 6%, is suffering particularly badly. Although it continues to gain market share from weaker rivals such as Burger King and Jack in the Box, its same-store sales fell by 2.8% in America in the third quarter and by 3% internationally. Investors are hopping mad about a 44% fall in the share price since Jack Greenberg became boss in 1998.

At its peak in 1996, McDonald's opened 2,000 new restaurants a year. It plans to launch just 600 in 2003 and it is closing 175 underperforming restaurants, quitting three countries and firing some 600 workers. Mr Greenberg refuses to accept that the group has gone “ex-growth”, pointing to opportunities in countries such as China (see article). But with four-fifths of its worldwide income coming from four mature markets—America, Britain, Germany and France—out of the 121 it is in, that allegation is proving hard to counter. Burger King is in even worse shape. Its price war, primarily against McDonald's (this week Burger King revived the 99-cent deal launched in September for its Whopper burger) has hit profits so hard that a planned sale by its parent, Diageo, fell through last month. Diageo is desperate to reassure investors that a sale will happen, even though one of Burger King's biggest franchisees this week went into bankruptcy.

The fast-food industry is, belatedly, responding to the new challenge. Peter Oakes, of Merrill Lynch, says Wendy's has bridged the gap between fast food and fast casual with a fresher menu and nicer ambience. McDonald's is not sitting still either. It is rolling out a new range of salad bowls and reintroducing its popular flatbread sandwiches. It has also bought or part-owns several fast-casual chains, including Chipotle, a Mexican-style grill with same-store sales-growth of 20%, Boston Market, a 650-strong chain vendor of “homestyle” meatloaf and chicken, and Pret A Manger, a British chain offering sandwiches, sushi and juices that is expanding in America. But none of this will deal with the weighty legal problem posed by the industry's biggest customers.

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Fast Chinese cuisine

Junk food?

Dec 5th 2002 | HONG KONG
From The Economist print edition

Why the future of fast food may be congee, tofu and roast duck

“EVENTUALLY, Chinese will displace the burger and the pizza,” says Michael Chan, chairman of Café de Coral, the world's biggest chain of Chinese-style fast-food restaurants. He does not mean in Hong Kong, his home market, where this has already happened, but in America, Europe and the world. It sounds brazen, but Mr Chan has supporters. In the Philippines, Tony Tan, chairman of Jollibee, the country's largest fast-food chain, has high hopes of Chowking, its young Chinese-food offshoot. As the only two fast-food tycoons anywhere to trounce McDonald's in their home markets, Messrs Chan and Tan deserve to be taken seriously.

Their optimism is based on two trends. One is growing health consciousness, as well as more acceptance of “ethnic” foods. In America, 90% of the fast-food industry is “western”—from Big Macs to doughnuts—and under 10% “oriental” (mostly Chinese). Mr Chan reckons that share could easily double as Americans who are too hurried for slow food but too worried by greasy burgers opt for a healthier alternative. Already, 90% of Café de Coral's customers in Canada, where it has dominated Chinese fast food since buying the Manchu Wok chain in 2000, and in America, where it is the second-biggest oriental chain, are non-Chinese.

Then there is mainland China, where fast food is booming. Today, barely 2% of all eating out in China happens in fast-food restaurants, compared with 32% in America, 25% in Japan, or 18% in Hong Kong. But the Chinese are getting richer and they see fast food as modern; the industry is growing by 20% a year. Most of this growth is today going to American fast food, not Chinese: McDonald's and, even more, Kentucky Fried Chicken (KFC). Mainland Chinese see the American chains as hip, new, even exotic. About 80% of the fast-food market is western. KFC already has almost 800 restaurants in China. McDonald's has over 500, and plans to open 100 a year.

In mainland China in the short term, Café de Coral, Chowking and other Chinese chains may find themselves selling fast-ice to Eskimos. They are betting that the novelty of the Big Mac will wear off and demand for western meals will slow—but that consumers will not lose their appetite for food delivered fast. Chinese food will satisfy that need. Mainland China may even come to resemble already-rich Hong Kong, where Chinese accounts for 70% of the fast-food market. Even in Shanghai, Colonel Sanders's finest chicken may not stay as finger-lickin' irresistible as it is now.

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Face value

Miss World war

Dec 5th 2002
From The Economist print edition

EPA

Julia Morley finds that managing a global brand is not easy

GONE are the innocent days when the Miss World contest existed largely to reduce search costs for ageing rock stars seeking future ex-wives. On December 7th this year's winner will be crowned in London—anti-pageant rioting that killed hundreds having prompted a last-minute switch from Nigeria—under a cloud from which the 51-year-old contest to find the world's “most beautiful” woman may never entirely escape.

Whatever other lessons may be drawn from this sorry tale, one is clear: it is not easy to succeed as a global brand. Unlike, say, American baseball's decidedly non-global “world series”, Miss World's ambitions literally reflect its name. Its website boasts of “a proven brand that's recognised globally”, over 2 billion viewers, “phenomenal” web hits and “consistently high-quality” programming. “If you're associated with Miss World 2002, you can be sure of one thing; it will be massively successful for your brand,” it promises would-be partners. Well, unless all publicity really is good publicity, that is no sure thing now.

It is wrong to blame Miss World for the riots, as did Ken Livingstone, London's mayor, when publicly regretting its relocation to his city. The blood of the dead is on the hands of the rioters, not those of Julia Morley, Miss World's chief executive, a self-described “tough bitch” whose late husband, Eric, held the first annual pageant of “international bathing beauties” in 1951.

Yet from the more humdrum perspective of global brand management, there is a case for Mrs Morley to answer. International businesses have no excuse for ignoring political risk. For sure, the “corporate social responsibility” brigade goes too far in its criticism of how multinationals operate in poor countries. But that does not mean any business can roll merrily into a place rife with corruption or religious fundamentalists without thinking through the risks to its brand—especially if the brand depends for its success on a positive reputation with customers. That is at least as true of Miss World as, say, Shell, which has long been troubled by the image of its Nigerian business.

Mrs Morley seems to have been astonishingly naive about political risk, and even more so about its subset, fundamentalist risk. A particularly fierce brand of Islamic fundamentalism has been taking root in northern Nigeria. Indeed, the sentencing of a Nigerian woman to be stoned to death after she had a baby outside marriage prompted several aspiring Miss Worlds to withdraw from the contest, and led to widespread calls for it to be cancelled or relocated. Instead, Mrs Morley seems to have concluded that the fundamentalists could be shamed into mercy by an act of global sisterhood. The “best way of supporting her”, she said, “is by going to the country, not by isolating it.”

A charitable interpretation might be that Mrs Morley was not really so naive. Perhaps she hoped that the desire of the Nigerian government to brush up its lacklustre international image by association with Miss World would outweigh its fear of upsetting the fundamentalists by quashing the death sentence. Even so, a cursory examination of Nigeria's recent history should have told her that her contest might inspire violent religious protests that could damage her brand by association. A local journalist may have triggered the riots by writing that, were he alive, the Prophet Muhammad might have married one of the contestants, but even without that, the fundamentalists might have found another excuse. Mrs Morley should have learned from a previous escape: in 1996, a feminist suicide squad threatened to set fire to themselves during Miss World in India. (An Indian man burnt himself to death outside the venue.)

It may seem cowardly; but when it comes to political and fundamentalist risk, discretion may be the better part of valour. Why expose your brand to Nigeria if you have a choice? Arguably Shell has none: the oil is there. But Miss World did.

Given all the talk of a clash of civilisations, might Mrs Morley deserve praise for fearlessly promoting western “culture”? Her pinning of blame for the riots on the Nigerian journalist and later the British media suggests not. Going to Nigeria may in fact have had more to do with the government's promises of support for the event than with any crusade for freedom.

The swimsuit issue

For perhaps Mrs Morley too felt she had no choice. Miss World is a global brand in crisis. Ever since feminists stormed the contest in London in 1970, it has been under attack in Britain as outmoded and sexist. It is no longer screened on networked British TV. Shunned by the elite, Miss World fell victim to brand schizophrenia. Mrs Morley wanted to add depth, coining the term “beauty with a purpose”; her husband favoured moving downmarket. The unhappy result in 2000, shortly after his death, was that contestants shared dreams of making the world a better place with Jerry Springer, a doyen of American trash-TV. There were plenty of viewers, but, since they were largely in poor countries, a measly demographic. Attempts to enter America have fallen foul of the dominant local rival, Miss Universe, part-owned by Donald Trump, a trashy tycoon.

On inheriting Miss World, Mrs Morley decided to move upmarket. The website boasts of a “brand new” Miss World, “reflecting the attributes of today's woman; a woman who has her own goals and views of her role within society”. Contestants are no longer expected to parade in swimsuits.

Maybe it was a desire to prove the character of this new Miss World that led Mrs Morley to take a political stand in Nigeria. Yet, although it may reflect badly on the state of the world, the brand might have fared better had she accepted Mr Trump's reported offer to buy her out. It seems unlikely that he would let Islamic fundamentalists anywhere near it—except, no doubt in their millions, via TV and the Internet. His answer to the brand identity crisis, one suspects: even skimpier swimsuits.

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Logistics

A moving story

Dec 5th 2002
From The Economist print edition

Companies are outsourcing huge chunks of what they do to logistics companies

WHAT caused ICI's share price to stutter briefly last week? Answer: rumours, no more, of logistics problems at a Dutch subsidiary of the British chemicals company. What is the biggest challenge facing Nokia with its new smartphones, which bring the power of a PC to a mobile handset? Answer: logistics, the Finnish company's ability to get all the parts into its mobile phones, and get the phones out to the market where and when they are wanted.

Logistics is a word that you see most often on the side of trucks. But it has a bigger meaning: the management of the flow of materials through an organisation, from raw materials to finished goods. “It's one of the most abused terms in business,” says Peter Bakker, boss of TPG, a transport group. The Oxford Dictionary definition of logistics is first, the “science of movement, supply and maintenance of military forces in the field.” Poor logistics helped to defeat Napoleon, and later Hitler, on the road to Moscow and Stalingrad: both over-stretched their supply lines. The same problem did for Rommel in North Africa, when his tanks lacked enough fuel to fight Montgomery effectively at El Alamein.

Much of the allies' Gulf war success was also attributed to logistics. Indeed, that war made logistics a sexy management subject. General Norman Schwarzkopf's logistics chief joined the American retailer Sears Roebuck, to work his magic in civilian life.

Ship-shape and Bristol fashion

Logistics might sound a simple enough business of moving things around, but it is growing more complex as customers demand more finely tuned services, and as new technology and greater use of the Internet open up new ways of passing around information. Now that companies have delayered, re-engineered and scrubbed the waste from their assembly lines, logistics seems worthy of rather closer attention.

Much of the Japanese-led methods of lean production and just-in-time supplies remained within factory walls. Incoming parts came in batches from warehouses, and sat around until they were used; outgoing products were delivered to distributors in batches, and also sat around. Now companies are more demanding, seeking to eliminate both incoming and outgoing inventory.

Now companies are more demanding, seeking to eliminate both incoming and outgoing inventory

They do this in several ways. To simplify what goes into the factory and make it more of a snap-together assembly line, they outsource more, and buy in sub-assemblies rather than individual parts. They are also trying to build only to orders from customers (known as BTO), rather than guessing what will be in

demand and supplying it from accumulated stocks. Cutting inventories and introducing BTO calls for a comprehensive, flexible freight operation. This is such a challenging task that companies are reluctant to do it all themselves. So more of them are, in effect, outsourcing logistics to third parties.

This movement is forcing the freight-transport industry to reshape, as customers seek service suppliers with global reach. Manufacturers want custom-designed delivery systems, using all types of transport—land, sea and air. Distinctions between postal, express and logistics services are blurring. And the fastest-growing part of the business is catering to the demand for outsourcing by providing companies with third-party logistics.

Companies realise that organising the supply of incoming parts and outgoing goods can account for 10% of their costs. Yet they know little about how best to do it, according to Mr Bakker of TPG, the world's second-largest logistics specialist (under its TNT Logistics brand). He says the biggest omission is not counting the cost of holding more inventory than is needed. Even car makers, for all their lean factories, produce cars that sit idle for up to 100 days.

Distinctions between postal, express and logistics services are blurring

Consolidators in control

Nowadays, with global supply-chains connecting cheap workers on one side of the world with rich consumers on the other, good logistics can make all the difference to a company's ability to serve its customers. It is not just what you make or how you make it. It is how quickly you get the parts together, or shift finished products from Asian factories to western markets. The success of retailers such as Wal-Mart in America or Marks & Spencer in Britain depends largely on getting the right goods to the right place on time. Indeed, one reason for M&S's tumbling profits a few years ago was that it lost control of its supply-chain; anxious to go farther afield in search of lower costs, it failed to maintain a system that could adapt quickly to what was selling and what was not.

These pressures are forcing consolidation in the freight industry, traditionally very fragmented. At one extreme are basic road-haulage companies, rail-freight firms, shipping lines or air-cargo firms. Above them is a handful of international companies known as “consolidators” or “integrators”. These are firms such as FedEx, UPS and DPWN (Deutsche Post World Net, which absorbed DHL). Such companies have lots of capital invested in their global networks, and they offer both parcel and express-delivery services. For the most part, they run standard services to make best use of their assets.

Other companies offer specialised services. Some act as dedicated contract carriers for clients, running their truck fleets. Others are freight forwarders, buying capacity on ships and cargo planes, and putting together loads from different companies to fill them. Then there are transport and warehouse-management firms, which organise the physical movement and storage of goods.

All such businesses deal with three parallel flows: physical goods, information and finance (leasing, lending, brokerage). As the business changes because the needs of shippers—ie, the ultimate customers, the companies that need their goods transported—alter, companies operating in one part of the chain are tempted to expand into others. They think the grass is greener over the fence. Thus freight forwarders, as well as doing basic tasks of arranging import documentation and booking space on ships, start organising the supply of parts and the preparation of kits for assembly. Some even stray into contract manufacturing for companies.

Management consultants at McKinsey calculate that the total American logistics market, which includes basic transport and in-house administration costs, is worth about $1 trillion a year, and grows annually by around 4%: in other words, it is a mature business. But the third-party market, of around $50 billion a year, is reckoned to be growing at 15-18%. On a similar narrow definition, McKinsey estimates that the European market was worth around $155 billion in 1999, and will expand to $213 billion by 2005.

The American logistics market is worth about $1 trillion a year

This growing market is being eyed, especially in America, by lots of existing freight companies. Most operators in one market, or one region, are considering widening their service and geographical footprint. Express air-carriers such as FedEx and UPS have the advantage of existing large networks, which they can also use for customised logistics. Broking houses such as Kuehne & Nagel can offer their skills in tying together different modes of transport. DPWN and TPG bring sheer size and capital. Truck-leasing firms, such as Ryder and Penske, and for-hire truckers, such as CNF and USFreightways, also have big

customer bases and fleet-management skills. One global manufacturer, Caterpillar, which makes construction equipment, has also chosen to enter the logistics business, hoping that its global distribution network will give it a good start.

The businesses that make most use of this level of logistics are in electronic components, consumer electronics (including mobile phones and PCs), pharmaceuticals, fashion and, above all, cars—both parts manufacturers and assemblers. Since the average car contains 10,000 different parts, some of them susceptible to competition from cheap manufacturers in low-wage countries, the industry tends to have extended supply-chains around the world. The conversion to lean manufacture in its factories has spurred a need for ever-more sophisticated logistics.

Smart and soft

So what exactly can smart logistics do for companies? One example is TPG's contract with Ford to service its Toronto factory. This plant produces 1,500 Windstar minivans a day. To keep it running virtually round the clock, TPG has to organise 800 deliveries a day from 300 different parts makers. Its software must be tied into Ford's computerised production system. Loads have to arrive at 12 different points along the assembly lines without ever being more than 10 minutes late. Parts must be loaded into trucks in a pre-arranged sequence to speed unloading at the assembly line. To make all this run like clockwork takes a team of ten computer-wielding operations planners and 200 unskilled workers, who make up the loads in the right sequence at a warehouse down the road. The vehicles involved are mostly owner-operated, but under contract to TPG. It is a seven-year contract, and TPG has to lower its price by 2% a year.

Another example is an arrangement between Maxtor, a maker of computer disk-drives, and Exel, the world's leading firm for pure logistics. Exel, formed from a merger of a shipping line and a road haulier, now owns no ships or trucks, focusing instead on logistics contracts. The Maxtor deal requires it to shift drives from factories in Asia to companies such as Dell, Compaq and HP in Asia and America, all within 48 hours. As John Allan, Exel's chief executive, says, “there is no inventory”.

For Mr Allan, the difference between pure logistics companies, such as Exel and TPG, and traditional freight firms is that “we analyse and optimise the supply-chain for the company and so create value.” He sees his role as orchestrating the supply chain. The rest of the industry are under his baton. One of Exel's biggest contracts is with Ford, for which it organises supplies for seven factories around Europe. Exel also works for Volkswagen in its operations in Spain and Mexico. The factory in Puebla, Mexico, turns out 1,400 new Beetles a day. And Exel helps with Nokia's logistics as well, especially in China and South-East Asia.

The more they get into orchestrating the flow of inbound goods, the sequencing of parts delivery and the management of supplier parks for vehicle assemblers, the closer these companies come to managing actual production. Along the supply chain, the different freight companies now increasingly do packaging, labelling and some manufacturing, especially in consumer electronics. TPG's TNT Logistics operation even does light assembly-work for DaimlerChrysler in America.

Some industry analysts reckon that in consumer electronics, the growth of such contract manufacturing, often organised through logistics companies, will lead to over a third of electronics manufacturing being outsourced by 2005. Some forecasters think that the share could then double again. Technology is partly driving this growth. According to a report by Accenture, advances such as the use of radio-frequency identification and the Internet could significantly improve supply-chain management. Transponders on product packages can communicate with devices in factories or warehouses, leaving a trail of where things are at any given time. All this makes it easier for manufacturers or their logistics contractors to track their products across the whole supply-chain. Accenture claims it is the biggest advance in supply management since the arrival of the bar-code.

Given these technological advances, and as logistics firms reach ever deeper into clients' core businesses, traditional manufacturing, whether of cars or personal computers, could start to disappear. The logistics operators may then organise everything but product development, design and marketing. Then they will be even more vital to the success of such companies as Nokia and ICI.

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European economies

What took them so long?

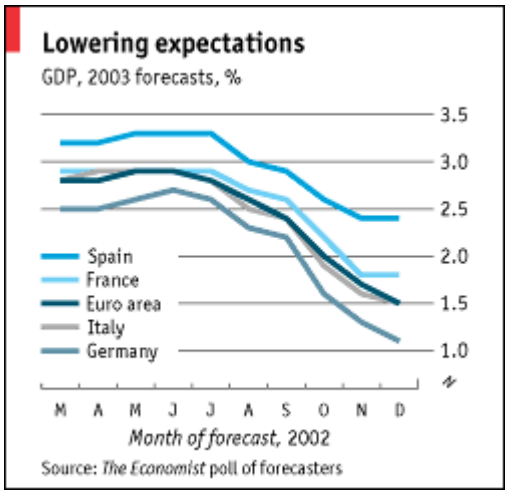
Dec 5th 2002 | FRANKFURT
From The Economist print edition

The European Central Bank shrugs off a year of inflation-phobia

CRITICS of the European Central Bank (ECB) have long complained that financial markets cannot tell what its officials are going to say next. The complaints have finally sunk in. As the ECB prepared to cut euro-area interest rates on December 5th, the first change in 13 months, the only question in bank watchers' minds, after so much official semaphoring, was the size of the cut. The ECB plumped for a bold half-point, to 2.75%, rather than a cautious quarter. That should stifle speculation that rates will soon fall further.

Since the bank's November meeting, when its customary "consensus" was harder than usual to reach, several members of its rate-setting governing council had hinted at a cut this time. Finally, on December 3rd, Wim Duisenberg, the ECB's president, talked unambiguously of strengthened evidence that inflationary pressures were easing, while "downside risks to growth" had not vanished. By central bankers' standards, the signal was deafening.

But why did the ECB leave rates unchanged for so long? By contrast, the Federal Reserve—despite America's higher growth rate—has been willing to cut on several occasions. This year, the euro area has seen one disappointment after another, most obviously in Germany, its biggest member. For instance, unemployment there rose by more than expected in November. In the third quarter, as in the second, GDP in the whole euro area grew by only 0.3%—or 1.2% at an annual rate. The future looks no cheerier. On average, the panel of economists polled monthly by *The Economist* now predicts growth of a mere 1.5% in 2003. Six months ago, our forecasters expected 2.9% (see chart).



Fiscal policy is doing little to support economic activity. The euro area's stability and growth pact requires members to keep their budget deficits to below 3% of GDP. A breach necessitates swift remedial action—or the offender may risk paying a hefty fine. The French government, it is true, seems to be defying the pact. No wonder, given that French growth slowed to a 0.8% crawl (at an annual rate) in the third quarter. France wants to cut taxes, even though the European Commission, which monitors countries' compliance, thinks it may break fiscal limits in 2003. But in Germany, where a deficit of 3.8% is likely this year, the government is raising taxes, to the fury of businesses and many voters.

The ECB's line has been unsympathetic—not only holding rates, but repeating in schoolmasterly tones the importance of sticking to the rules. The commission recently proposed adjustments to the pact: but the 3% limit would stay, and countries with structural deficits, such as Germany, would still be expected to tighten policy, even in bad times.

One reason for the ECB's slowness, thinks Mark Wall of Deutsche Bank, is institutional. Unlike the Bank of England, it takes no votes (or has so far admitted to none); nor does Mr Duisenberg dominate the governing council as Alan Greenspan does the Federal Reserve's open-markets committee. Consensus is the rule—and a consensus for change can take time to build. Second, and perhaps more important, the

ECB's treaty-prescribed duty is not to keep the economy at full steam but to maintain price stability, which it defines as a rate of inflation of no more than 2%. Despite the weakness of the euro-area economy and talk of the risk of deflation, that target has proved hard to hit.

In October inflation in the euro area was a stubborn 2.3%, up from 1.9% in July. Core inflation, which excludes energy, food, alcohol and tobacco prices, has been 2.4% or thereabouts for several months. But evidence of weakening activity has been building for months, and economists expect the slowdown, perhaps with help from a stronger euro, to pull inflation below 2% next year.

The main reason for inflation's stickiness, suggest economists at Goldman Sachs, is that unemployment in the euro area has risen only slightly—to 8.4%, from a low of 8% last year—as the economy has slowed. That has meant little downward pressure on wages. In turn, that has kept inflation in services on a rising trend, reaching an annualised rate of 3.5% in the three months to October. Moreover, slack in the economy affects inflation in services only slowly. Assuming that output dropped below capacity in the second half of 2001, the economists reckon that inflation in services should be about to turn.

Not surprisingly, wage moderation is a virtue that Mr Duisenberg preaches frequently. Wage stickiness could stop inflation falling much below 2%, and could justify the expectation of many economists that short-term interest rates will fall no lower than 2.75%.

That is hardly good news for those who would welcome easier money. But in a club of 12 diverse countries, not everybody wants lower rates. The 2.3% average for October hides a broad range, from 1.3% in Germany—where the figure has since fallen further—and Belgium, to 4%-plus in Ireland, Portugal and Spain. In Germany, where some see a risk of deflation, the case for lower interest rates is plain. Yet Rodrigo Rato, Spain's finance minister, said this week that, with credit growing by 13% a year in his country, a rate cut would be “not so great”. The ECB will never please everybody. Nor has it tried to.

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Wall Street

Address unknown

Dec 5th 2002 | NEW YORK
From The Economist print edition

Lost or buried e-mails earn only the gentlest of slaps for investment banks

ONE common lesson emerges from the Microsoft antitrust trial and the continuing investigation into investment banks: e-mails are a legal nightmare. How much, a clever company might wonder, would it cost for them to go away? One plausible estimate is $1.65m. That is the amount being paid by Goldman Sachs, Morgan Stanley, Citigroup's Salomon Smith Barney, US Bancorp's Piper Jaffray and Deutsche Bank, to settle a joint investigation by the Securities and Exchange Commission, the National Association of Securities Dealers (NASD), and the New York Stock Exchange (NYSE) into charges of destroying e-mails—or making them inaccessible to regulators.

They got off lightly compared with the $100m fines that other firms have paid this year, largely on the basis of embarrassing e-mails whose existence they preferred not to deny or argue about in court. But they can hardly draw comfort that this will have much impact on more serious investigations into conflicts of interest on Wall Street.

The puny e-mail punishment does little more than suggest that the firms had less than perfect record-keeping standards. Regulators offered no justification for the fines, other than saying that they are a record for this kind of book-keeping violation. Oddly, even though the three regulators split the investigation, they will not disclose which of them investigated which firm. Surely, as a matter of public policy, the prosecutor and the defendant in a legal action should be identified, particularly if two of the investigators (the NASD and the NYSE) are funded by those they investigate and the third is not.

These important issues pale before the most ludicrous aspect of the settlement: it avoids describing what each firm did, and it prescribes the same penalty for each. A firm could have fallen foul of the rules surrounding the retention of e-mails either by failing to preserve them, or by simply not having them in an accessible place. Redressing the latter requires patience; the former cannot be redressed at all. Goldman Sachs, for example, says that not a single e-mail was lost or destroyed: all have been recovered, albeit with a delay which regulators found inappropriate. Piper Jaffray says it retained “large volumes of e-mails”, which by inference suggests not all of them. The firm declines to comment further.

The most curious case is that of Morgan Stanley, which played a pivotal role underwriting Internet companies during the bubble. Somehow it has managed to avoid being dragged through the e-mail quagmire, unlike its peers Citigroup, CSFB and Merrill Lynch. Cynics, of which there are an increasing number around Wall Street, wonder whether there was some magical difference in Morgan Stanley's systems. The company is adamant that there was no intentional destruction of records, but e-mails were, apparently, “lost”. How many is not clear, and Morgan Stanley declines to comment. So far, so good: until we learn otherwise, it seems to be cheaper to destroy the e-mail and pay the fine.

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EU enlargement

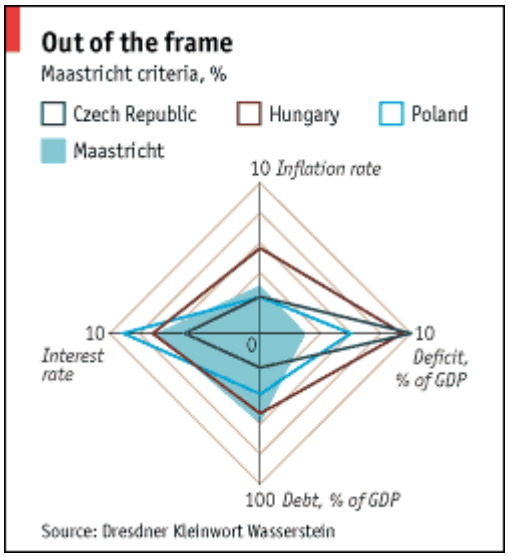
What convergence?

Dec 5th 2002 | WARSAW
From The Economist print edition

Central Europe's candidates love the Union but fear the euro

WITH European Union enlargement apparently steaming ahead, the bond markets are pricing in "convergence" as if it were a done deal. Moody's, a rating agency, recently upgraded the foreign-currency debt of the eight Central European candidates. The process of integration with the EU was now "virtually irreversible," it said. Not so fast.

Negotiations for entry in May 2004 are due to be wrapped up at the Copenhagen summit next week. Then each candidate must hold a national referendum—most likely with positive results. But they now seem less anxious to get to the next stage after accession: adoption of the single currency, which is obligatory for new members. That is because they will have to fulfil the strict Maastricht criteria for levels of inflation, budget deficits and public debt. Several EU hopefuls have already breached the budget deficit ceiling of 3% of GDP (see chart). Standard & Poor's, a rating agency, recently downgraded Poland's and Hungary's increasingly burdensome long-term domestic debt.



The European Commission and the European Central Bank have given warning that hasty euro entry could endanger the applicants' growth prospects by depriving them of the monetary flexibility needed to cope with the pressures of the single market. Even some rich West European countries have been harmed by the single currency, with interest rates too high for sluggish Germany, but too low for buoyant Ireland, for example.

Until recently, candidate states would not have dared to question openly the rules underpinning the single currency, lest the markets send their currencies plunging and their borrowing costs spiralling. But stinging comments on the "stability and growth pact" from within the EU have given some the courage to complain. György Suranyi, a former governor of Hungary's central bank, declared last month that, if the EU adopted a more flexible fiscal framework, Hungary's growth prospects would doubtless improve.

Poland's government still insists that it will be ready to join the euro in 2006 or 2007. But last month Grzegorz Kolodko, its finance minister, presented his EU counterparts with proposals to loosen the fiscal rules. He argued that budgetary rules should apply to the aggregate deficit in the euro-area, rather than to each country—an extension of a British proposal. One Dutch official fumed privately that profligates would be "free-riding" on the backs of more frugal countries. But Mr Kolodko is unrepentant: "the EU should think about Italy or Belgium's public debts—not to speak of their levels on the eve of EU and [euro-zone] accession." These are bold words, although they would carry more weight if Poland's awesome budget deficit was itself designed to stimulate economic growth not to put off reforms.

Most analysts doubt that Central Europe's biggest countries—Poland, Hungary and the Czech Republic—have a chance of meeting the 3% deficit limit by 2007. Having secured their places in the EU, these governments may be even more inclined to let budgets and borrowing rip, delaying euro entry as late as 2010. By that time the stability pact may no longer exist, and new members may be able to enter on looser criteria. Punters betting on speedy convergence may have jumped the gun.

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Lazard

Bruce's big bet

Dec 5th 2002 | LONDON AND NEW YORK
From The Economist print edition

Is Lazard's expansion killing the culture that made it rich?

BRUCE WASSERSTEIN, boss of Lazard for nearly a year now, wants you to know that his firm is anything but a boutique. It may be small, but the investment bank—founded over 150 years ago—has a presence in America and Europe, a big asset-management business, and a renowned restructuring team. Guided by Mr Wasserstein, the firm has moved away from its patrician, if sometimes chaotic past. To be sure, some of the changes were long overdue, especially for a firm that last year seemed to be on its deathbed.

Mr Wasserstein has centralised Lazard's operations, which had long been divided among independent entities in Paris, London and New York, and forced stroppy partners to work together and share information on deals. He has also simplified the bank's byzantine shareholding structure. The terms of his contract make him unchallenged supremo—not a form of corporate governance being recommended elsewhere. He is now spending millions on new talent that is likely to change the firm beyond all recognition.

Does Lazard need such a radical cure? For those who believe in old-style relationship banking and independence of merger advisory work, Mr Wasserstein is Lazard's undoing. Others think that he is right to hire dynamic new bankers with big pay packets at a time when talent is available, and to aim beyond Lazard's traditional business. Lazard used to be a shop of clever individualists who worked as much against as with each other. It would not have been wise to send them off on the same duck shoot, recalls Marcus Agius, Lazard's deputy chairman in London, since they would probably have ended up shooting each other.

The cost of Mr Wasserstein's remedy is unpredictable. So far, he has spent an estimated $100m, most of it on a big bet that the market for mergers and acquisitions will revive. But if the market remains depressed until 2004, at least—as many think it will—Mr Wasserstein may need even more capital to finance his ambitious plans. He is said to have put in several hundred million dollars of his own money. Without an upturn in M&A work, the firm has only another 18 months before more capital is needed, reckons one banker.

With his brash style, Mr Wasserstein has already alienated many of the old guard. Felix Rohatyn, a Lazard veteran, who once brought in a third or more of Lazard's merger-advisory business, played a pivotal role in the recent takeover of Household International, an American consumer-finance company, by HSBC, a global bank based in London. But this time he was acting under the banner of Rohatyn Associates, a one-man shop. Mr Wasserstein also sacked six managing directors at the firm's London branch in July, all of them old-style relationship bankers. They were given a week to vacate their offices—a far cry from the old days when Lazard's lay-offs were gentler.

Those who are brought in with fat pay packages care little about radical changes to Lazard's culture. Chuck Ward left CSFB with a promise of guaranteed pay of $7m a year. So far Mr Wasserstein has added 24 new partners, with more to come. Many of them are 30-something MBA-toting industry experts. None of them can replace the highly connected, politically savvy (and often independently wealthy) advisers who have left in recent years. These days, Lazard bankers are as likely as those from any other firm to overwhelm clients with pitchbooks and slideshows, the stock-in-trade of the management consultant. Mr Wasserstein's recent moves appear to take Lazard ever closer to the soup-to-nuts universal-banking model, which aims to offer clients everything from cheap loans to asset management and industry expertise, as well as strategic advice.

The timing is, to say the least, contrarian. Universal banking is out of favour with regulators as well as

distrustful clients. A sudden new awareness of these firms' conflicts of interest has made Lazard's traditional approach look more of a winning formula, with its emphasis on impartiality. Would it not make more sense now to strengthen the firm's identity, rather than copy everybody else?

One of Lazard's remaining strengths is its restructuring business in America, which is being transplanted to Europe. About 60% of Lazard's fees, expected to fall to $250m this year, come from restructuring work. Much of the rest of the firm's revenue will come from the pending acquisition of Pharmacia by Pfizer, an American drug giant, a client brought in by Mr Rohatyn years ago. Recently, Lazard appeared to have mended fences with Vivendi, a long-time client that was formerly run by Jean-Marie Messier, a Lazard alumnus. But its mandate was only to sell a stake in the Vivendi Environnement subsidiary—the parent company still wants nothing to do with Lazard.

None of this will matter much in the medium term, if Mr Wasserstein—with a track-record as a brilliant dealmaker in America—can find a rich buyer for Lazard itself. As the second-biggest shareholder after Michel David-Weill, the non-executive chairman, Mr Wasserstein is estimated to own around 10-15% of the bank's shares. Lazard's market value may now be around $2.5 billion. If he can sell Lazard for something like its value of a few years ago, he might earn even more than the $650m he took home from the sale of his investment-banking boutique, Wasserstein Perella, to Dresdner Bank in 2000. But how useful could a bulked-up Lazard be to a rival financial firm? Grey-suited gigantism is yesterday's story.

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Retail banking

Citi slickers

Dec 5th 2002 | DüSSELDORF AND TOKYO
From The Economist print edition

Local banks are struggling, so what is Citigroup doing right?

SIMILARITIES between the ailing economies of Germany and Japan are a hot topic, particularly in banking and insurance. Japan's banks are undeniably in worse shape than Germany's: some of their balance sheets are propped up by little more than regulatory indulgence. German banks are desperate to cut costs, perhaps by merging—this week a union of two of the biggest, HypoVereinsbank and Commerzbank, was rumoured.

Both banking industries have to cope with a distorted retail market. So why are the retail arms of America's Citigroup doing well in both countries? At Citigroup Japan—which celebrated its 100th birthday this year—the retail division pulled in profits of $928m in the financial year to March, twice what it made two years before. In Germany, Citibank Privatkunden boasted a cost-income ratio of just 44% in the first nine months of 2002, 40-50% below those of big private banks' retail operations.

In Japan, Citi enjoys much lower funding costs than stricken local institutions. It has also benefited from depositors' fears that their money is not safe with local banks—which are weighed down by ¥150 trillion ($1.2 trillion) of bad debts—despite the fact that deposits at Japanese banks are covered by a government guarantee until March 2005, while those at foreign houses, such as Citi, are not. This summer it was even rumoured that Tokyo's provincial government, one of Japan's biggest depositors, might shift some money to Citi.

In both countries, the bank has tightly controlled costs. In Japan it has a mere 24 retail branches, augmented by telephone and Internet banking and, since 1999, by a deal giving it access to the post office's 26,000 cash dispensers. It uses newspaper advertisements rather than salesmen to push its products. In its 300 German branches, Citibank Privatkunden strives not to waste costly labour on mundane tasks. Customers feed money-transfer forms (the main way Germans pay their bills) into scanning-machines rather than hand them to a teller. Peter Buschbeck, a board member, says that branch staff spend 50% of their time with customers, compared with an industry average of 20%. Customers asking for a loan can expect an answer within 20 minutes.

Being in the right businesses also helps. Consumer finance, a Citigroup speciality in America, has been a hit. Although the risks are higher than in plain retail banking, so are yields. Citigroup now has Japan's third-largest consumer-finance business, with loans of an estimated ¥1.7 trillion. In Germany, the big private banks have shied away from consumer finance—although HypoVereinsbank is now stirring itself. Savings banks, being restricted to local markets, lack scale. That has left the field clear for the likes of Citibank Privatkunden, the market leader, Volkswagen Bank and CC Bank (owned by Spain's Santander Central Hispanico).

In credit cards, Citi's Japanese earnings may have tripled between 1999 and 2001, according to Morgan Stanley. The German arm is also making headway, despite Germans' preference for debit cards. The two retail banks have also avoided certain activities, such as business lending—not their area of expertise, they say—and have thus avoided the bad corporate loans that have hobbled some German banks and crippled Japanese ones.

Easy money, then? Not exactly, although Citigroup has been helped by the locals' failings. Good judgment counts, for example, in assessing the riskiness of consumer loans. Luck counts too: with both the German and Japanese economies getting deeper into trouble, consumers may soon borrow less and default more. Will the Citi formula keep working then?

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Crédit Lyonnais

Long arm of the law

Dec 5th 2002
From The Economist print edition

American prosecutors have empanelled a grand jury to indict Crédit Lyonnais

Get article background

WHILE rival suitors circle Crédit Lyonnais in France, its past is catching up with it in America. Jeffrey Isaacs, an assistant United States attorney in Los Angeles, has started long-awaited grand-jury hearings to indict the bank for fraud in connection with its purchase in 1991-93 of Executive Life, an American insurance company. Several witnesses have been called and more will appear this month and next. An indictment is expected early next year.

After Executive Life went bust in 1991, insurance regulators chose a rescue package put together by Crédit Lyonnais. As part of the deal, the bank arranged for a new insurance company, Aurora, to take over Executive Life's insurance contracts. Regulators were told that a consortium set up to own and manage Aurora would be independent of Crédit Lyonnais, as both federal and state laws required. However, the bank had confidential agreements to buy back shares in Aurora from consortium members, who were acting as fronts for the bank.

As Crédit Lyonnais was then owned by the French state, Mr Isaacs has, in effect, been seeking the indictment of a foreign government ever since announcing his plans in May 2001. French diplomats and politicians have been lobbying in Washington for a settlement. They have argued that the crime was victimless, perpetrated by a few bad apples, long since departed.

It is not clear why Mr Isaacs has been given the go-ahead now. However, the clamour to indict those responsible for frauds at Enron and WorldCom may have made it increasingly difficult to let Crédit Lyonnais off the hook. An indictment may be a formality, but a trial is not. Before any indictment is made public, the French are likely to mount a final push in Washington to see off a criminal case. These hearings will weaken their hand, however. Several Crédit Lyonnais managers, past and present, may not have a happy new year.

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South Africa

A roller-coaster ride

Dec 5th 2002 | JOHANNESBURG
From The Economist print edition

The rand's rebound against the dollar is a mixed blessing

LAST year South Africans gnashed their teeth as the rand lost over a third of its value against the dollar. Rich whites moaned that there would be no more holidays abroad or fancy foreign cars; more seriously, the poor watched food costs rise, as prices of oil, transport and imported grain all surged. President Thabo Mbeki told a judge to lead a commission to investigate the rand's collapse. Some blamed instability in neighbouring Zimbabwe; others faulted the sluggish pace of economic reform. Johannesburg was thick with rumours of wicked plots by traders and investment banks to sell the currency short. Some even accused the world's financial markets of racism. Trevor Manuel, the finance minister, blamed "little twerps" in London for trading against the rand.

Yet the rand has bounced back this year (see chart), outperforming just about every other currency as the dollar has weakened. By the end of November it had gained 22%, against a basket of other currencies, since the start of January. It is much stronger now, at 9.15 to the dollar, than it was last December, when it briefly touched 13.5. Even last week's terror attacks in Kenya (and a small bomb by white extremists in South Africa) failed to scare traders away. Local newspaper headlines that once wept now crow that South Africa is on top of the world.

Why the revival? The central bank has raised interest rates four times since January to fight inflation that now tops 14%; booming revenues from exports and tourists have helped too. And even though Zimbabwe's woes have deepened, they show little sign yet of spreading to South Africa. Renewed global interest in gold may also have tempted traders to believe that the rand will do well. And most people anyway believed the currency had sunk too far last year.

But, though a stronger rand will dampen inflation, it is not all good news. Those flourishing sales of South African cars, wine and textiles that were boosted by a weaker rand will now be hampered by a stronger one. Exports and higher tourist numbers helped the country to post a modestly respectable 2.6% annual rate of growth in GDP this year, says Mr Manuel.

This week he said he was "exceedingly optimistic" thanks to the rand, and that growth will surge higher next year, above 3.5%. But that will be hard to deliver if overseas sales slow, and higher interest rates start to bite. Nor will all investors be reassured by a surging rand. Although outsiders may like a strong currency, a stable one is more important. Roller-coaster rides—down or up—make business returns unpredictable.

So Tito Mboweni, governor of the central bank, will want to keep things as steady as possible, perhaps letting the currency now devalue gently. Last week the bank's monetary policy committee left rates unchanged, but it may cut them as early as March if inflation starts to drop. Around that time the government plans to sell a chunk of the monopoly fixed-line telecoms company, Telkom, which could attract still more foreign currency, bolstering the rand. But neither a slump nor a surge would really be welcome next year; rather, South Africans should wish for less interesting times.

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India

Currency teaser

Dec 5th 2002 | DELHI
From The Economist print edition

A strong rupee is giving policymakers a new sort of headache

THE Indian finance ministry's mid-year review, released this week, sees the external sector as a silver lining around the country's huge fiscal deficit. “Buoyant” and “encouraging” are the words used to describe three consecutive quarters of current-account surplus—the first in a quarter-century. Add to that swelling foreign-exchange reserves and a stronger rupee, and some are arguing that it is time for drastic liberalisation of India's foreign-exchange regime. They could be disappointed.

For most of the past decade, the nominal value of the rupee has been allowed to decline gently against the dollar, by about 5% a year, thus staying fairly steady in real terms. This year, however, it has been appreciating in real terms (and, since June, nominally as well). It would have done so more sharply had the central bank not been buying dollars with gusto. Exporters of manufactured goods, obsessed with price competition from China, are aghast at the rise—and at the prospect held out by some forecasters that a sustained boom in India's IT exports means it will continue.

The rupee's recent strength is only partly related to India's prowess in software and the mushrooming of “business-process outsourcing” in such projects as call-centres. The chunky surplus on invisibles owes more to remittances: non-resident Indians, attracted by the stability of the rupee and its higher interest rates, have been moving their offshore deposits back home. Similarly, Indian companies are borrowing more in dollars without selling rupees forward to hedge repayments. The trade deficit, meanwhile, has been shrinking, as imports grow slowly.

The inflows have boosted foreign-exchange reserves by some $20 billion this year, to $66 billion, or 12 months'-worth of imports. The size of this cushion has triggered some calls for further liberalisation of the labyrinthine foreign-exchange controls that India still maintains, despite the move in 1993 towards rupee convertibility for trade purposes.

In recent months, some controls have duly been eased. It is now simpler, for example, for individuals to open foreign-currency bank accounts, and for travellers to get hold of foreign exchange. And non-resident Indians have been allowed to take out money acquired through inheritance, or from rents and dividends.

Some commentators have taken all this as a harbinger of full capital-account convertibility. That is not on the cards. The experience of 1991, when India ran out of money, has left the central bank prone to caution—an approach it felt was vindicated by the East Asian crisis of 1997-98. With war in Iraq looming and a turbulent oil market, some risk aversion is understandable. India's fiscal deficit—some 10% of GDP and widening—is another reason for moving slowly. Just as one rating agency, Moody's, is considering upgrading India's external debt, another, Fitch, has warned that its local-currency rating is under threat.

Nor is it certain that opening the capital account would mean a weaker rupee. It might even attract more capital inflows. As India's exporters are learning, convertibility is a two-way street.

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Economics focus

Does population matter?

Dec 5th 2002
From The Economist print edition

Countries at the right stage of development can reap a demographic dividend

EVER since Malthus's apocalyptic vision in 1798 of overcrowding and starvation, a debate has raged over population growth and its links with development. The latest contribution, a report* by the UN Population Fund (UNFPA), argues that larger families and fast-growing populations obstruct development and perpetuate poverty by slowing growth and diverting consumption away from the poor. In the 1980s, if all countries had cut net fertility by five births per thousand women, poverty would have been reduced by a third, the report claims. It concludes that, to overcome poverty, countries must deal with population concerns and fight poor reproductive health, unwanted fertility, illiteracy and discrimination against women.

How does population change affect the economy? Views have shifted in the past few decades. The 1960s and 1970s seemed to favour the neo-Malthusian view that high fertility hindered development: people with many children were unable to save and had to spend more on health and education, hindering investment in physical capital. Such pessimism spawned many publicly funded family-planning programmes, which were touted as a panacea for poor countries' economic ills.

In the 1980s, however, economists, not social scientists, came to dominate the population debate, with revisionist results. Empirical research seemed to discredit the neo-Malthusian view. Human capital and technical change, rather than physical capital accumulation, were the main drivers of growth. The revisionists argued that population pressures ultimately provoke institutional, technological and policy changes. Population growth, they concluded, has little impact on growth, unlike such factors as bad policies, corruption and lack of natural resources.

Over the past few years, economists have been reverting to the view that population does indeed matter. So is Malthus making a comeback? Not exactly. The important thing, says the UN report, is a changed age structure of the population, rather than population growth itself. People are living longer and, as parents realise that children have better chances of survival, fertility rates are falling, leading eventually to a higher ratio of working-age adults to dependants. Moreover, as family size declines, more women are likely to enter the labour market.

So long as the labour market can absorb more workers, production per head will increase. This creates a “demographic dividend” of growth, making possible higher savings and investment. Parents with fewer children can invest more in their health and education, creating a more productive workforce. So the source of population growth and its timing are of the essence: at early and late stages of the demographic transition—when the youngest and oldest age-groups are growing the fastest—growth suffers. The demographic dividend appears only in the middle phase.

This also means there is only one window of opportunity. Low fertility eventually leads to a rising proportion of older people, raising the dependency ratio as the working population goes from caring for children to caring for parents and grandparents. Nor is the demographic dividend automatic. The right policies—a flexible labour market, investment and saving incentives, provision of high-quality health care and education—are still essential to making the working-age population more productive.

Provided that is done, a change in the population's age structure, due to a drop in mortality and fertility rates, will promote growth. But what about poverty? Higher growth helps to reduce it but, according to Robert Eastwood and Michael Lipton**, having fewer babies also changes the distribution of consumption in favour of the poor. A drop in the birth rate eventually affects the supply of workers—unskilled workers in particular since fertility is usually higher among the poor—which in turn can help to increase

employment and wages. Fewer babies can also mean a second income, as mothers can then join the labour market.

Asian miracles

This demographic dividend was essential to East Asia's economic success. In 1950, the typical East Asian woman had six children. Today she has two. As a result, between 1965 and 1990, the working-age group rose from around 57% to over 65% of the total population, increasing four times faster than the number of dependants. Some estimates suggest that the demographic dividend accounted for around a third of the growth in the region's income per head in that period. Latin America, on the other hand, has not benefited in the same way. Although demographic conditions were favourable, income per head grew by an average of only 0.7% per year between 1975 and 1995, compared with 6.8% for East Asia. This is due to poor policies: studies suggest that had the region been more open to trade, average growth would have more than doubled.

If these observations are correct, developing countries entering their demographic transition have a unique chance to cash their population dividend. South Asia will reach its peak ratio of workers to dependants between 2015 and 2025. Richer Latin American countries have completed the transition, but poorer ones continue to lag; their peak is likely in 2020-30. In sub-Saharan Africa, however, only 11 countries are expected to reach that stage before 2050, and a lot still has to be done to reduce fertility levels. The rapid rise in AIDS deaths will also frustrate changes in age structure that would otherwise occur. And once the transition is over and the dividend pocketed, countries will face the next big challenge: how to care for the old.

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*"State of the World Population 2002; People, Poverty and Possibilities: Making Development Work for the Poor", UNFPA

**In "Population Matters. Demographic Change, Economic Growth and Poverty in the Developing World", edited by Nancy Birdsall, Allen C.Kelley and Steven W. Sinding, Oxford University Press, 2001.

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Nanotechnology

Trouble in nanoland

Dec 5th 2002
From The Economist print edition

Plagued by both pessimism and hype, can nanotechnology grow up?

“HUMANITY, get down on your knees”, scream the billboards advertising “Prey”, the latest novel by Michael Crichton, author of “Jurassic Park”. The horrible beasties threatening humanity in this new thriller are not giant dinosaurs, but swarms of minute “nanobots” that can invade and take control of human bodies. Nanobots are putative machines with working parts that are smaller than 100 nanometres (billionths of a metre). A film is, inevitably, in the offing. And to increase the impending nano-horror, the chief scientist at Sun Microsystems, Bill Joy, is due next autumn to publish a book fleshing out his own nano-Luddite views. In an article in *Wired* two years ago, Mr Joy pleaded for a moratorium on all nanotechnology research.

All this attention has some scientists worried, and not without reason. Last summer, a report issued by a Canadian environmental body called the action group on erosion, technology and concentration took a swipe at nanotechnology. It urged a ban on the manufacture of new nanomaterials until their environmental impact had been assessed. The group is better known for successfully campaigning against biotechnology, and especially against genetically modified crops. Given that the well-organised and influential biotechnology industry has suffered some serious setbacks at the hands of such activists, some worry that the embryonic nanotechnology industry will be a pushover.

One study already under way aims to assess the health risks of nanotubes. At present, these cylindrical, carbon-based molecules are nanotechnology's favourite building-block. The research, led by a group at the National Aeronautics and Space Administration's Johnson Space Centre in Houston, has found in preliminary studies that inhaling vast amounts of nanotubes is dangerous. Since they are, in essence, a form of soot, this is not surprising. But as most applications embed nanotubes in other materials, they pose little risk in reality.

Small fortunes

At the opposite end of the spectrum are the nano-enthusiasts, who are recklessly setting impossibly high expectations for the economic benefits of nanotechnology. A widely-cited estimate for the size of the nanotechnology business in ten years' time is a trillion dollars—a figure seemingly plucked from the air.

Lured by such large numbers, and always on the look-out for the next big thing, venture capitalists are

fervently courting nanotechnologists. But as one pundit put it, so far there are more meetings on investing in nanotechnology than there are serious opportunities to punt. Investors are finding that business plans are often little more than repackaged research-grant proposals. And many of the top “nanotechnology” companies are actually developing more conventional microsystems.

The lack of a clear definition of nanotechnology is hampering meaningful discussion. A hard-core definition would restrict the field to machines that have functional parts on a scale of less than 100 nanometers. At present, little can live up to this. No wonder enthusiasts favour a liberal definition that covers anything involving nanometre-scale particles.

This definition covers particles used to make skin creams more transparent and ski wax more slippery. It also includes anything based on nanometre-thin layers of materials. These may be light-emitting layers in semiconductor lasers, or ultrasensitive magnetic films in the heads of magnetic-disk storage systems. Nanotubes also make the grade, whether they are used in flat-screen devices, in strengthening composite materials or in storing hydrogen.

The problem with such a broad definition is that there is no common relationship among all these examples, whether in their method of fabrication or in the markets they are aimed at. Another difficulty with defining nanotechnology is that, unlike biotechnology, the field does not stem from one established academic discipline.

Such a lack of clarity is not stopping America, the EU and Japan from vying to outspend each other on nanotechnology. Politicians have been successfully sold the idea that nanotechnology is the industrial revolution of the 21st century. The nano-spending race began with America's national nanotechnology initiative, launched two years ago, which will bring some $700m to the table next year. Meanwhile, the EU has earmarked $1.2 billion for nanotechnology in 2003-04. Japan plans similar levels of investment.

Upping the ante, a bill was introduced in the American Senate in September to establish a federal nanotechnology agency to be called the National Nanotechnology Research Programme. This would create a permanent bureaucracy, based in Washington, DC, to ensure that nanotechnology funding remains firmly in the budget for years to come. In other words, nanotechnology seems here to stay.

A small step for man?

The irony is that nanotechnology is still a long way from living up to the expectations of either optimists or pessimists. A recent *tour de force* of molecular manipulation provides a good gauge of how far the new industry has got.

Reporting in the journal *Science* two weeks ago, Don Eigler and his team at IBM's Almaden Research Centre in Silicon Valley reveal that they have built molecular-scale logic gates—the basic ingredients for a computer. The construction involved painstakingly pushing individual carbon-monoxide molecules across a copper surface using a scanning tunnelling microscope (essentially a sharp metal tip). By aligning the molecules in a zigzag pattern and then gently pushing one molecule, they produced a molecular cascade, rather like a falling row of dominoes. Setting up several criss-crossing rows of molecules, the team was able to build basic computing devices.

Dr Eigler's cascades are neither a health hazard nor, for the moment, worth investing in. Although much smaller than existing electronic devices, it takes about five minutes for each molecular domino to fall: an excruciatingly slow speed. It also has to be kept in an ultra-high vacuum and at ultra-low temperatures. It is worth comparing this prototype of a molecular machine with Dr Eigler's initial efforts at single-atom manipulation, 12 years ago. He was able to coax a few xenon atoms to form an IBM logo, to the amazement of the scientific world (and to the bafflement of everybody else).

In many new technologies, it is common to overestimate what can be done in five years' time, and to underestimate what can be done in 50 years' time. Dr Eigler and other optimistic nanotechnologists must hope this rule of thumb applies to nanotechnology as well. However, there is a huge technological gap between molecular cascades and fully-functional nanobots. The rest of the world, then, should not hold its breath.

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South Africa and AIDS

No more denial

Dec 5th 2002 | JOHANNESBURG
From The Economist print edition

A new report shows exactly who is infected with HIV

Get article background

GOOD data make good policy, as South Africa's politicians like to say. But deciding how best to fight AIDS requires knowledge of exactly whom it afflicts. Activists, academics and the United Nations have long insisted that there is plenty of evidence about AIDS in South Africa. But the government has always demanded more detail. President Thabo Mbeki is personally affronted by the idea that Africans might be seen as "sub-human" carriers of disease, and so is especially demanding.

Safer sex is catching on

Agreeing on that information is tricky. Last year, the politicians duly rubbished a study by the Medical Research Council, which showed fast-rising deaths among the young, especially women. The council blamed AIDS illnesses. The government said that an independent rise of tuberculosis or pneumonia might be responsible. Since doctors and family members rarely admit that a patient has died of AIDS, nobody trusts death certificates. And making calculations from high levels of infection among women who are pregnant is difficult. These tell you only about young women who have had unprotected sex and become pregnant.

Now years of fruitless wrangling should be over. On December 4th Nelson Mandela launched the most authoritative report so far. In 2002, researchers from the Human Sciences Research Council interviewed 10,000 people of all races, ages, incomes and locations, and conducted confidential oral-swab HIV tests on 8,428 of them. Their results are relatively good news. HIV infection for 15-49-year-olds was previously put at about 20%; the new study says it is 15.6%. Overall, that suggests 4.5m infected people (some 11.4%).

Another surprise is that some provinces have lower levels of infection than expected. Recent antenatal surveys in KwaZulu-Natal showed that 33.5% of 15-49-year-old women had the virus. The new study puts it at just 19.5%. This is more persuasive than antenatal surveys, because it included women who are not pregnant, and also went beyond clinics in densely populated areas, in which infections tend to be higher.

Most encouraging, though, is the fact that South Africans are well informed about AIDS. Some 80% are sure, unlike Mr Mbeki, that HIV causes AIDS. And young people aged between 15 and 24 are changing their sexual behaviour. Young people have long been thought to be particularly vulnerable to the disease. But fewer young people than expected are having sex, and 23% say they have given it up altogether. And 29% said they had not had sex in the 30 days before being questioned. Of those who had, most report only one partner in the past year. Crucially, around half use condoms, a high level that matches countries such as Uganda, where HIV infection levels are dropping.

Can you trust all these answers? Yes, say the researchers. Interviews were strictly confidential, and levels of infection by age corroborate what these young people are suggesting: they are less likely to be infected than their elders.

This week, the researchers briefed ministers on the findings. They are not likely to be delighted by all of them. Over 95% of respondants want AIDS sufferers and infected pregnant women to get anti-retroviral drugs, which the government resists. Only just under half think the government spends enough fighting

AIDS.

The survey also shows that income and education have no bearing on the chance of infection, so Mr Mbeki's emphasis on fighting poverty to tackle AIDS seems misplaced. Most disturbing, though, is that children are worse affected than previously thought. Around 6% of those aged between two and 14 have HIV—a level four times higher than suspected. And children now head 3% of South African households.

Will the government attack this report? It seems unlikely. The researchers have been astute to team up with Mr Mandela, whose political clout should prevent much official meddling. And the scale and thoroughness of the research is without parallel. The government now has some good data. Roll on the good policy.

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Medical technology

Down the tubes

Dec 5th 2002
From The Economist print edition

Need a new artery? Grow your own

ANY structure, however well built, suffers wear and tear over the years. In the human body, it is not merely some of the main organs that can go kaput, but also the plumbing system: arteries and veins. Finding replacement plumbing is not yet as simple as buying a length of copper tube, however. But two new techniques for growing replacement arteries may make life easier for surgeons.

At the Georgia Institute of Technology, Raymond Vito and his team have been experimenting with “distraction angiogenesis”. This involves implanting a mechanical device that stretches an existing section of an artery, known as the gastroepiploic artery, which is located below the stomach. The device uses hydraulically driven rollers to lengthen the artery. Pressure is released by withdrawing fluid via a subcutaneous port with a syringe.

According to Dr Vito, the artery responds with remarkable alacrity. In only a month, it can create a surplus section up to 30cm long that can be removed and implanted wherever it is needed. Indeed, the gastroepiploic artery seems almost to have been designed with just such a procedure in mind. The artery varies in diameter, so surgeons can stretch different sections—depending on the diameter they are looking for. Better still, it is usually disease free, even in patients who have vascular disease elsewhere in their bodies.

Dr Vito believes that this artery would happily yield to being stretched, snipped and rejoined several times over. Another possibility would be to have the artery stretched in advance, and frozen, in expectation of future procedures. Dr Vito is, in short, providing living proof that the way to a man's heart is through his stomach.

In California, meanwhile, Cytograft Tissue Engineering, a research company in Novato, is developing more elaborate techniques for growing new blood vessels. The company uses the novel approach of sheet-based tissue engineering. At present, most tissue constructions rely on encouraging cells to divide and grow on a scaffold—to give the tissue shape.

Instead, the company grows flat sheets of fibroblast cells (the basic building-blocks of most connective tissues), and then simply rolls the sheet into a tube around a steel rod. The key to the technique is a culture medium that stimulates cells to produce their own glue, in the form of collagen and other binding proteins.

After the steel rod is removed, the artery is completed by seeding its inner walls with a layer of cells that form the lining of blood vessels (these are harvested from a patient's own blood or veins). So far, the engineered grafts have been successful in animals for periods of as long as 90 days. Further studies are planned.

According to Todd McAllister, a researcher with Cytograft Tissue Engineering, it may in a few years' time be possible to create arteries which, by incorporating layers of other cell types (including genetically modified cells), are actually stronger than native veins and arteries. Such super-arteries would not be developed simply out of scientific hubris. They would be invaluable candidates for arterio-venous shunts, ie, connections made between veins and arteries in dialysis patients to increase blood flow. Synthetic vessels are often used for such patients, but they rarely last longer than a few months before being compromised by leaks, clots, infection and clogging.

Human trials of the basic technology may begin in as little as 18 months' time. If they are successful, the procedure might even become commercially available in only three years' time. If Dr Vito and his team

manage to commercialise artery stretching, though, approval by America's Food and Drug Administration would only require approval of the stretching device. Home-grown arteries do not, after all, involve the implantation of foreign tissue or substances.

Either way, both technologies hold great promise for the hundreds of thousands of patients who are facing coronary bypasses, or even the loss of a limb due to deteriorating blood flow. In commercial terms, then, such research may certainly have hit a rich vein.

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Genomics

Modest mouse

Dec 5th 2002
From The Economist print edition

A draft sequence of the mouse genome has been published

Get article background

Building a better mouse

NOT as famous as Mickey, nor as troublesome as Jerry, perhaps: the latest mouse to capture attention has the prosaic name C57BL/6J. That is the strain of laboratory mouse whose genome sequence has just been published.

The international mouse genome sequencing consortium and allied groups present their work in a bevy of papers in this week's issue of *Nature*. The centrepiece is the draft sequence of the roughly three billion nucleotides—the quartet of molecules that make up DNA—that is the genome of a mouse. Celera Genomics, of Rockville, Maryland, has already sequenced a draft mouse genome, but it is available only to customers paying some $15,000 per year.

The mouse genome is useful because of its similarity to the human genome. Mice and people both have about 30,000 genes, and 90% of the genes associated with inherited human diseases are also found in mice. So one can do all sorts of potentially valuable tests on laboratory mice that will aid in the understanding of human diseases, say through studies that either remove, or add, copies of these genes in mice.

Having a published version of the mouse genome could help researchers investigating the progress of diseases such as Down's syndrome. This is caused when humans inherit an extra copy of the 21st chromosome. It is not clear how having this extra stretch of DNA causes the disease. But research published alongside the mouse genome identifies many of the murine genes that correspond to human genes on chromosome 21. By tagging these at an early stage in a mouse's development, researchers should be able to work out what tissues such genes have a role in forming in mice. Thus, it should be able to draw conclusions about the purpose of equivalent genes in humans.

Another paper discusses a new form of gene mapping. This should help speed up the discovery of sets of genes that control complex traits such as diabetes. The researchers compared long stretches of murine DNA—which is easier to work with—while searching for one-letter differences between individuals that may indicate the location of a gene. Researchers hope that the results will generalise to humans.

What, by the way, is next to be sequenced? Chickens, chimpanzees and honeybees.

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Classical music on CD

Full of surprises

Dec 5th 2002
From The Economist print edition

Two remarkable young pianists crown the year's best classical recordings

FAR from being mediocre or narrowly predictable, the most interesting releases of instrumental, orchestral and contemporary music in 2002 prove the remarkable vitality of classical music today.

Two young pianists produced outstanding discs for EMI. A 23-year-old Macedonian, Simon Trpceski, made his debut with a recording of Russian music, while Leif Ove Andsnes, a Norwegian, turned his attention to the music of his fellow countryman, Edvard Grieg. Mr Trpceski's programme encompasses some of the most challenging music in the repertoire—sonatas by Scriabin and Prokofiev, and Stravinsky's sadistically demanding arrangement of Three Movements from “Petrushka”. But this disc is more than a display of pyrotechnics. Even in the densest of the Stravinsky pieces, Mr Trpceski demonstrates a magnificent control of line and structure. In Mikhail Pletnev's transcription of a Concert Suite from Tchaikovsky's “Nutcracker” he releases all the charm and magic of the music, and reveals the real depth of his musicality.

Mr Andsnes's fascinating disc of a selection of Grieg's Lyric Pieces could not be more authentic: a Norwegian pianist playing Grieg's 1892 Steinway in the composer's villa in Troldhaugen. The recording beautifully captures the intimacy of the venue and the delicacy of the instrument, and Mr Andsnes's playing catches the improvisatory fantasy of these sophisticated and delightful miniatures. Yet there is nothing small-scale about the emotional or expressive range they encompass, from the dream-like Phantom and Illusion, to the grotesque March of the Trolls.

Dvorak's Slavonic Dances are familiar as individual numbers, often played as encores or musical *amuse-bouches* before the main event of a concert. But Nikolaus Harnoncourt's Teldec release of the Op. 46 and Op. 72 sets, with the Chamber Orchestra of Europe, makes a case for them not just as important parts of Dvorak's output, but also as integrated cycles of pieces.

Another Teldec release presents an even more involved and emotional musical cycle: Harrison Birtwistle's Pulse Shadows. The work interleaves nine pieces for string quartet with nine settings of the poetry of Paul Celan. The soprano soloist is Claron McFadden, and the players are those masters of contemporary music, the Arditti Quartet and the Nash Ensemble, conducted by Reinbert de Leeuw. Each of the 18 pieces is a separate, self-sufficient fragment. Yet they all inhabit an extreme emotional world, and listening to the whole cycle is a disturbing and enriching experience. The final string quartet piece, Todesfuge-Frieze 4, encapsulates the expressive world of the whole work. The music is accompanied by a ghostly halo of harmonics, which is typical of the interplay between images of darkness and light that

dramatises the whole cycle.

Death also looms over another remarkable release of contemporary music: Gérard Grisey's Quatre Chants Pour Franchir le Seuil (Four songs to cross the threshold). This setting of ancient texts and modern poetry was the last piece that Grisey composed before he died suddenly in 1998. It is played on this Kairos release by Klangforum Wien with Catherine Dubosc singing and Sylvain Cambreling conducting. Each movement seems to suspend time, in both the slippery, glittering textures of La Mort de la Voix (The death of the voice) and the storm music of La Mort de l'Humanité (The death of man). The warped clockwork of the final movement, Berceuse, is a vision of a new kind of time, as if death had been overcome, and the threshold crossed; this music ends one of the most moving recordings of recent years.

Mahler's Fifth Symphony is another work that conquers death, moving from the funeral march of its opening movement to the unstoppable counterpoint of its finale. The piece was the climax of Sir Simon Rattle's first concert as artistic director of the Berlin Philharmonic Orchestra in September. EMI's rush release of the CD of this thrilling performance captures the intensity of the relationship between the orchestra and their new director. The Berlin players give themselves to the music as do few other orchestras, and the sheer power of their playing is overwhelming. Sir Simon's interpretation is no less convincing, as the drama of the earlier movements culminates in the outrageous energy of his performance of the finale. This release suggests the beginning of a sensational partnership between Sir Simon and the BPO; like all of these new discs, it swells the heart and gives cause for hope.

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Opera on CD

Stage thrills

Dec 5th 2002
From The Economist print edition

The best new CDs are live recordings

KARITA MATTILA, Anja Silja and Eva Randova—a mighty European trio—come together in a thrilling recording of Janacek's “Jenufa” (Erato). Made just over a year ago at the Royal Opera House in London, with Jorma Silvasti and Jerry Hadley as the rival stepbrothers, Laca and Steva, and conducted by Sir Bernard Haitink, this is not only one of the finest recordings of this opera, but a vivid example of how—with such a distinguished cast—theatre can be successfully recreated on disc.

Rossini's “Elisabetta, Regina d'Inghilterra” (Opera Rara) was given a gala concert as part of the queen's golden jubilee celebrations. The CDs, recorded the same week, have Jennifer Larmore giving an all-out portrayal of the Virgin Queen, with the men in her life given sterling voice by Bruce Ford, as Leicester, and Antonino Siragusa—a young Italian tenor to watch—as Norfolk. Giuliano Carella conducts the London Philharmonic. This is early Rossini, with a story that is short on accuracy but a feast for *bel canto* enthusiasts.

Sir John Eliot Gardiner and the English Baroque Soloists with the Monteverdi Choir performed Gluck's “Alceste” (Philips) in Robert Wilson's production in Paris. “Alceste”, Gluck declared, excited him “to a frenzy”. Anne Sofie von Otter in the title role, with Dietrich Henschel and Paul Groves, bring all the experience of the stage production to this reading, achieving a faithful nobility of utterance that is essential to Gluck's lean, expressive drama.

Sir Charles Mackerras conducted a searing concert performance of Mozart's “Idomeneo” at the Edinburgh festival in 2001, preserved here on the EMI label, with Ian Bostridge as the youthful, almost romantic, hero. As his son, Idamante, Lorraine Hunt Lieberson proves again that she has few equals as an interpreter of 18th-century trouser roles and that “Idomeneo” can easily equal Mozart's more frequently-heard masterworks.

Ancient Greece is also the setting of Offenbach's “La Belle Hélène” (Virgin), but in purely burlesque style. Dame Felicity Lott as Helen of Troy, with Les Musiciens du Louvre-Grenoble conducted by Mark Minkowski, show why this became one of the season's hottest tickets when Laurent Pelly's production was at the Châtelet Theatre in Paris.

From the archives comes a moving document, “Leontyne Price Rediscovered” (RCA). This is a Carnegie Hall recital from 1965, her first there, and has an exciting sense of occasion. Singing a repertory from Handel to Samuel Barber and Lee Hoiby, Ms Price demonstrates the true art of the prima donna. Finally, it was Emmanuel Chabrier, who, according to Ravel, changed the direction of French harmony. “Musique Adorable” (Hyperion) is a collection of Chabrier's complete songs, performed by Graham Johnson and a group of soloists including Geraldine McGreevy, William Burden, Toby Spence and Stephen Varcoe. A treat to be savoured.

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Spanish imperial history

They rose to conquer

Dec 5th 2002
From The Economist print edition

THE Spanish empire stretched from California to Patagonia and from Florida to the Philippines. One of the many virtues of Henry Kamen's book is to remind us how much, in the early centuries at least, kings of Spain thought of their empire in European terms. They were concerned to hold on to the prosperous territory that had been acquired by Ferdinand of Aragon—Naples and the Sicilies, Milan and Lombardy, Burgundy and the Netherlands. The American colonies were important only in so far as they provided the bullion, sugar and other marketable commodities that paid for the armies, alliances and ordnance to defend the European empire.

Isabella of Castile and Ferdinand of Aragon who started it all were a devoted couple who travelled incessantly around their kingdoms during the 30 years of their joint reign. This, of course, witnessed the pivotal year of 1492, when Granada was taken from the Moors (largely through internal squabbles among the Muslims and some astute negotiating by the Iberian Christians), and that obscure Genoese, Christopher Columbus, made his landfall in the Bahamas thinking he was near India.

Spanish soldiers were very highly regarded at that time. But Mr Kamen stresses that they were always a minority in the armies that won the European campaigns. Engineers from other countries manufactured all Spanish armaments, northern bankers provided the credit and foreigners made up a large part of the civil service.

Spain's was the first overseas empire, won by adventurers, few of whom were military professionals or from the aristocracy. Unlike other Europeans, most Spaniards were not sailors or shipbuilders, so that Spanish navies were always weak and it was remarkable that so many treasure fleets crossed the Atlantic unscathed.

Mr Kamen is a historian of Spain in Europe, and his accounts of the American conquests are patchy—for the executions of the two Incas, Atahualpa and Tupac Amaru, he ignores all eyewitness accounts and uses only the fanciful Garcilaso de la Vega and Guaman Poma. He thinks that Cajamarca, an Inca provincial centre, was Atahualpa's “capital city” and makes many other minor errors and omissions. Although Bishop Las Casas's condemnation of Spanish brutality is discussed, there is no mention of Charles V's important debate about the spiritual validity of conquests—which led to the banning of all expeditions in the Americas between 1549 and 1560.

Some would argue that Mr Kamen makes too much of cruelty and overwork as the causes of population decline of American indigenous peoples. He does note Noble Cook's view that 90% of the demographic catastrophe came from imported diseases, but ignores the collapsed birth-rate caused by social disruption.

“Spain's Road to Empire” is a monumental work, elegantly written and very readable. Most of the sweeping generalisations are thought-provoking and valid, but some can be peculiar: the Indians in the Jesuits' Paraguayan reductions had skirmishes against the Portuguese, which leads Mr Kamen to the odd conclusion that “without the amazing prowess of the Guarani soldiers, the power of Spain in South America could have been extinguished.” The book's weakness is that it tries to cover too much, from the unification of Spain to the 18th-century revitalisation of the empire under the French Bourbon kings. It is a history of kings and battles and treaties. There are very competent summaries of the campaigns and

Spain's Road to Empire: The Making of a World Power 1492-1763
By Henry Kamen

To be published in America as "Empire: How Spain Became a World Power, 1492-1763" by HarperCollins in March 2003
Allen Lane/The Penguin Press; 609 pages; £25.

Buy it at
Amazon.com
Amazon.co.uk

diplomacy of Charles V, Philip II, the Thirty Years War, the wars of the Austrian and Spanish succession and the other conflicts that drained Spain's resources. All of that is important as background, of course, but as a comprehensive roadmap to the empire this book, unfortunately, is far from clear.

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By Henry Kamen.
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Modern fiction

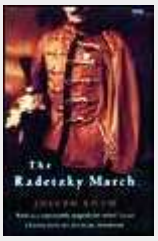
Fathers and sons

Dec 5th 2002
From The Economist print edition

IN A lull at the battle of Solferino in 1859, the young emperor, Franz Joseph, asks for a spy-glass to survey the field. Aghast, an infantry lieutenant, Joseph Trotta, hurls him to the ground as French and Italian marksmen open fire on the figure who has so foolishly identified himself as the Austrian commander. Trotta, the son of a Slovene watchman, takes a bullet in the shoulder. In gratitude, the emperor promotes and ennobles him. So opens one of the gravest and grandest of all 19th-century novels written in the 20th century.

The story traces the varying fortunes of the Trotta family. The hero of Solferino, a stranger to the social heights, grows eccentric. His son, a cautious district commissioner, lives dutifully in the paternal shadow, hoping that his own son, Carl Joseph, a well-meaning but feckless young officer, will somehow justify the newly glorious Trotta name.

The Radetzky March
By Joseph Roth and Translated by Michael Hofmann



Granta Books; 363 pages; £14.99

Buy it at Amazon.co.uk

The action takes place mainly outside Vienna, in the provinces and borderlands of a weakened multinational empire, though there are also worldly set pieces in the Austrian capital. The story unfolds with a blend of accident and ineluctability, the military march, from which the book takes its name, recurring at points as a leitmotif. Although the cast of secondary characters is large—Demant, a Jewish military doctor, Carl Joseph's several women friends, and Chojnicki, a sceptical live-for-today Polish count—and although the empire's clock is forever ticking down on the mantelpiece, the emotional heart of the book is about fathers and sons.

The material is often poignant, but never heavy or depressing. Roth can evoke an unknown place and time with an exactness of sensory detail that is particularly alive to sounds and to changing light. His sharp but sympathetic wit is present throughout, and scene after scene is brightened by unexpected, comic detail.

The author of this masterpiece was born in 1894 in Galicia on the Austro-Hungarian empire's north-eastern border with Russia. Roth studied philosophy, served in the 1914-18 war (embellishing his military exploits) and worked afterwards as a journalist, chiefly in Berlin. His wife and his father, whom he never knew, went mad. A Jew, Roth fled Nazism in 1933, sheltering in Paris where he drank himself to an early death, in preference, as he put it, to suicide.

“The Radetzky March” came out in 1932. Michael Hofmann, the translator of this new English edition, warns us in a fine introduction that the novel is in many ways untypical of Roth's other books, many of them looser, more open-grained satirical urban novellas. Mr Hofmann worries that if we read “The Radetzky March”, we will stop there, sated by its magnificent range and conclusiveness. Well, some readers may. But others will surely want to explore further a writer of such astonishing capacity.

A nostalgic monarchist, Roth mourned the collapse of the Austro-Hungarian empire. He lived with a sense of familial and historical loss and a dread of instabilities to come. In the father-figure of the emperor, Roth wanted to find a principle of order amid the decline of old ideals and the growing violence of class and national conflict. That wish for a benevolent and omniprotective parent was a political and emotional fantasy, as Roth himself ruefully understood—but perhaps also an inescapable fantasy of a kind that all of us at some level share. It was Roth's genius to put a universal theme into a historical novel that retains all its power in our own not-so-post-imperial age.

The Radetzky March.
By Joseph Roth.

Translated by Michael Hofmann.
Granta Books; 363 pages; £14.99

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Swordsmen and swashbucklers

Three, and more

Dec 5th 2002
From The Economist print edition

PANACHE, the quality so dear to Edmund Rostand's swashbuckling hero, Cyrano, is displayed with almost equal flamboyance by Richard Cohen, a former Olympic fencer, as he springs from branch to branch of his prodigious subject.

Mr Cohen focuses on the small university town of Leuven, not far from Brussels, as the home of the greatest collection of fencing books. Most were written in the 16th century, at a time when even Martin Luther was happy to endorse the art of swordplay as an exercise beneficial to both mind and body.

Weaving history and anecdote into a seamless tapestry, Mr Cohen is at his best in his account of the inglorious period of French history when duelling was treated as an extension of courtly entertainments, with no room for those who did not have a properly illustrious background. Small wonder, as Mr Cohen observes, that Voltaire, driven into exile for daring to challenge one of these exalted creatures, thought that Louis XIV's greatest achievement was the banning of duels.

Inactive readers, unversed in the significance of *quinte*, *flèche*, or *prises de fer*, will find much to enjoy here, even as they painlessly acquire a surprising amount of information about swordplay. Most irresistible, perhaps, are Mr Cohen's accounts of the women who have excelled as fencers. The heroine of Arturo Perez-Reverte's wonderful novel, “The Fencing Master”, was a fiction; inspiration may have come from Julie d'Aubigny, known as *la Maupin*, a ferocious beauty, who used her fencing skills to demolish rival suitors for any woman she fancied.

Escaping imprisonment in the Bastille to become mistress of the Elector of Bavaria, *la Maupin* made her debut at the Paris Opera in 1690 before retiring to a convent where she died at the age of 37. In a book filled with less colourful histories than this, her life would, without doubt, overshadow all competition; here, it features as part of a vivid and hugely enjoyable pageant of extraordinary tales.

By the Sword: A History of Gladiators, Musketeers, Samurai, Swashbucklers, and Olympic Champions.
By Richard Cohen.
Random House; 416 pages; $29.95.
Macmillan; £20

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Evolution

The grand view

Dec 5th 2002
From The Economist print edition

A master of evolution takes a last long look at Darwin

STEPHEN JAY GOULD was no lightweight, physically or intellectually. This vast book, the last one he published before he died in May, unveils his distinctive vision of evolutionary biology—as it should be, as it is, and as it has been.

The Structure of Evolutionary Theory
By Stephen Jay Gould

Harvard University Press; 1433 pages; $39.95 and £27.50

Buy it at
Amazon.com
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Gould's strategy is to identify a Darwinian essence, the logical core of Darwin's own doctrine, and chart its history. Gould takes that essence to be a three-part thesis about natural selection. The first is about the agency of natural selection. Natural selection almost always acts on individual organisms. In a population of competing individuals, organisms better suited to their circumstances are more likely to survive and reproduce, thus passing their superior characters to their offspring. Since fitter organisms produce more offspring, over time the nature of a population changes. For Darwin, selection almost never acts on groups or species, and harmonious relations in nature are just the side-effect of individual struggle.

The second is about natural selection's efficiency. “On the Origin of Species” established the fact of evolution, but Darwin's fellow biologists were by no means convinced that evolutionary change was driven by natural selection. How did it explain novelty? It is easy to see how natural selection weeds out unfavourable mutations and preserves favourable features. But how can selection be a creative force? Darwin has a good answer to this challenge: natural selection builds novelty incrementally.

The third is about selection's scope. Natural selection acts on individuals. A particular population of possums may be subject to predation by cats. As a result, larger individuals in that population are fitter and the population average changes. But how do changes like this—microevolutionary changes—relate to the history of life revealed by paleobiology? That history reveals patterns, some of which, the domination of terrestrial flora by the flowering plants, for example, are vast in space and time. Others are more local. When the Americas were joined, life flowed both ways, but far more northerners invaded the south than vice versa. How are local events in particular populations related to these macroevolutionary patterns? The jaguar penetrated South America and replaced local predators. For Darwin, macroevolution is just microevolution aggregated over long periods of time and space.

Gould goes on to chart the fate of Darwin's ideas. His aim is to identify continuing challenges to these three central themes of Darwin's picture: challenges that persist today in a transformed but still recognisable form. For Gould thinks there was something importantly right about these critical responses. And while he certainly does not present himself as calling for the destruction of Darwin's cathedral, he does see himself as arguing for major revisions and extensions of that edifice.

Consider, for example, the creativity of natural selection. Natural selection can make novel structures, but only if certain conditions are satisfied. Selection can shift a population from life in the trees to life on the ground by tiny steps—but only if the right kind of variation is available. Variation must be abundant. Selection on an arboreal ape population will be impotent if variations which improve their terrestrial prospects are sparse. As apes change from tree-dwellers to ground-dwellers, much must change. Variation in one characteristic must be independent of variation in other characteristics. If, say, hand shape could not change independently of foot shape, selection could not make back feet suitable for walking while leaving the ape with usable hands.

So for Darwin to think that natural selection explains major evolutionary innovations, he had to bet on the amount and kind of variation that typically exists in lineages. That wager has been controversial ever since Darwin made it. Gould's bet, based on recent work in developmental biology, is that Darwin was not quite right. Sometimes the supply of variation is as Darwin needed it to be. But variation is often constrained by the fundamental mechanisms of development. These constraints make some evolutionary transitions easy and others more difficult. The history of life shows great innovation, but great conservativeness too. The most fundamental features of animal bodily organisation have been largely unchanged for the last 500m years or more.

Gould also urges major revisions to Darwin's other core ideas. He has long been famous for thinking that species appear suddenly (at least, by a geologist's standards), are stable for most of their existence, and then disappear by extinction or splitting into daughters. This is part of his case for thinking that there is a very complex relationship between evolution in particular populations and the patterns we see in the history of life. Gould's views on the scope of natural selection are linked to his views on agency. Selection does act on individual organisms. But it does not act on them alone. Species, groups and even genes are agents. Life is organised into a hierarchy, and selection can and does act at every level of that hierarchy.

The protégé of one of the great 20th-century palaeontologists, George Gaylord Simpson, Gould's instinct is to turn to the long patterns of fossil history. He has often been challenged by biologists and ethologists, notably Richard Dawkins, who are more impressed by selection's adaptiveness than its conservatism. Though not alone, Gould is the spearhead of a minority view. Inevitably bulky, given its scope, his book is so bloated by asides, digressions, polemics and hobbies that it is positively obese, and this makes it a hard book to review justly. It is far from fair in its treatment of the many biologists who do not accept Gould's theory as a package. In many ways it is enormously irritating. But it is also a book of great power, scope and learning. In the end, its impressive features far outweigh its irritations. It is a book that one would expect to read and reread, for Gould articulates and defends a distinctive vision of the agenda of evolutionary biology; of the mechanisms of evolutionary change; and of the relationship of evolutionary biology to its own past. Despite its occasional unfairness to others and its tics and twitches, there is, indeed, a certain grandeur to this view of life.

The Structure of Evolutionary Theory.
By Stephen Jay Gould.
Harvard University Press; 1433 pages; $39.95
and £27.50

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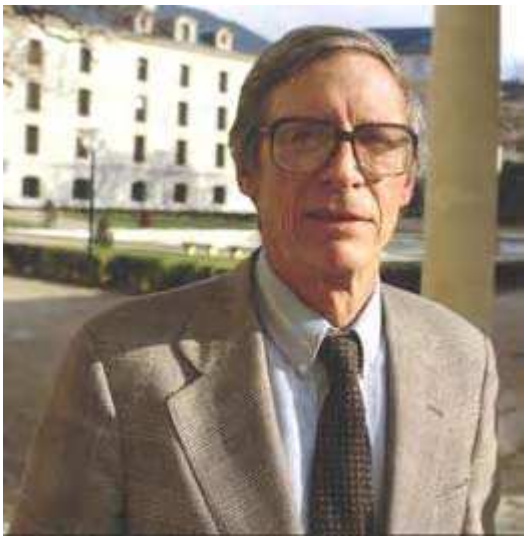
About sponsorship

John Rawls

Dec 5th 2002
From The Economist print edition

John Rawls, political philosopher, died on November 24th, aged 81


Katz

WHEN young, John Rawls was a talented athlete. Instead of becoming one of America's most distinguished political thinkers, he could have been a baseball player. Thin, quick and gangly, he would have made a perfect third baseman, a position requiring lightning reflexes and no time to think.

In the line he chose, however—close argument—Mr Rawls was a slow mover. He noted queries in pencil, responded to every objection and often begged for time with, "I'll have to think about that." Many philosophers treat their theories as extensions of themselves; his seemed more like a common enterprise. He was modest, claiming that he took up philosophy because he was not clever enough for music or mathematics. Others at his level were quicker. Few were as thorough.

The germ of "A Theory of Justice", the book that to his surprise made him famous, began to circulate in draft soon after he reached Harvard from Princeton and MIT in 1962. By the time of its publication in 1971, Mr Rawls had done his best to work in answers to every possible objection. His assiduity made the book hard-going. It also meant that it met a test proposed by Hilary Putnam, a logician and colleague, for a philosophical classic: the smarter you get, the smarter it gets. The book has sold getting on for 400,000 copies, and exists in dozens of languages, most recently Arabic.

In "A Theory of Justice", Mr Rawls attempted to lay out a defendable basis for an equality-minded liberalism. Its pillars were two principles of justice: the inviolability of individual rights and the idea that when justifying social inequality—some degree of which was inevitable in a flourishing and prosperous society—absolute priority should be given to the needs of the worst off. By putting rights back at the centre of the enterprise and by re-invoking the old idea of a notional social contract among putative equals, Mr Rawls did much to free political theory in America and Britain from apparent cul-de-sacs. It also encouraged philosophers to think more practically about moral issues in the public arena.

Problems of redistribution

Challenges were not long in coming. Much fire was concentrated on Mr Rawls's famous "veil of ignorance": what principles of justice would we choose, he asked, if we did not know our talents, wealth or opinions? Would we be as risk-averse as he seemed to think? This eye-catching device actually mattered less to the whole than it looked. A more notable attack came from Robert Nozick (who died in January). In "Anarchy, State and Utopia" (1974), Nozick argued that Mr Rawls's two principles of justice were in irreconcilable conflict. Attempts at redistribution to correct for inequality were bound, Nozick believed, to infringe on personal freedoms.

Conservatives took up Nozick's charge with alacrity. Though socialists were lukewarm to Mr Rawls, the two men were soon represented outside the academy as prizefighters for right and left: in the blue corner, Nozick, in the red corner, Rawls.

For all its importance, the issue of redistribution arose for Mr Rawls from a deeper concern. How can people with conflicting ideas about morals, religion and the good life agree to principles that will allow them to live together in a decent society? Though the need for toleration is perfectly general, because of America's divided history and his own family background, Mr Rawls felt its demands with unusual acuity.

He was born to a wealthy, professional family from Maryland, a slave-owning border state that stayed in the Union during the civil war. The father was a Baltimore lawyer who, to the son's chagrin, shared the racial bigotry of his class and time. His mother campaigned for women's rights.

Mr Rawls grew up with a powerful conscience. Though not conventionally religious, there was something deeply moral about him. At one time, he thought of becoming a minister of religion. Colleagues remember his kindness and wry humour. He was almost universally admired, even loved. Not all of us can be so good, of course. Isaiah Berlin, an Oxford political thinker, referred to him teasingly as Christ. Political opponents chided Mr Rawls for overplaying human decency and underestimating our selfishness. A conservative writer called him an innocent.

Holier than some might wish, perhaps. But innocent, never. In 1943, Mr Rawls signed up as an infantry private and fought on the Pacific beaches. A rare example of direct political action was his protest in 1945 against the Hiroshima bomb. Like his reconciling hero, Abraham Lincoln—whose memorial he visited on trips to Washington—Mr Rawls appealed to our better natures. But he knew from experience what people and states were capable of. Not to see this darker, more pessimistic side is to mistake what he was about.

In his later work, Mr Rawls paid more attention to “how” questions of fair process and tried to extend his principles from what struck some as their unduly western, not to say American, context. He lived behind a veil of privacy with his wife and four children, accepting few honours, giving few interviews and devoting spare time to hiking and sailing.

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Overview

Dec 5th 2002
From The Economist print edition

America's manufacturers seem dubious about the recovery. After a string of upbeat indicators at the end of November, the ISM's manufacturing index rose only to 49.2 in the month, from 48.5 in October. ISM readings above 50 indicate expansion, while those below 50 indicate contraction; the manufacturing index has been below 50 for three months in a row. The ISM's service-industry index was more upbeat, however, rising from 53.1 in October to 57.4 in November.

The **euro area's** economy grew by a sluggish 1.2% at an annual rate in the third quarter. Unemployment crept up to 8.4% in October, from 8.3% in September. In November, the euro area's economic-sentiment index, which measures both industrial and consumer confidence, fell to 98.6—its lowest in a year—from a revised 98.8 in October. Falling consumer confidence outweighed rising industrial confidence.

Unemployment in **Japan** returned to a record high of 5.5% in October, up from 5.4% in September. Deflation continued as consumer prices fell for the 37th consecutive month. Industrial production fell again in October, by 0.3%.

Canada's economic growth slowed in the third quarter, to a 3.1% annualised growth rate. This was less than America's growth during the same period.

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Output, demand and jobs

Dec 5th 2002
From The Economist print edition

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production	Retail sales (volume)	Unemployment % rate	
	1 qtr*	1 year	2002	2003	latest	latest	latest	year ago
Australia	+ 3.5	+ 3.7 Q3	+ 3.6	+ 3.3	+ 2.7 Q2	+ 5.4 Q3	6.0 Oct	7.0
Austria	+ 2.5	+ 0.9 Q2	+ 0.6	+ 1.6	– 1.9 Sep	+ 0.4 Aug	4.1 Oct	3.8
Belgium	+ 1.2	+ 0.8 Q3	+ 0.6	+ 1.7	+ 1.3 Sep	– 6.5 Sep	11.6 Nov†	10.8
Britain	+ 3.4	+ 1.8 Q3	+ 1.6	+ 2.5	– 2.5 Sep	+ 6.0 Oct	5.3 Sep††	5.1
Canada	+ 3.1	+ 4.0 Q3	+ 3.4	+ 3.2	+ 5.5 Sep	+ 7.0 Sep	7.6 Oct	7.4
Denmark	– 3.8	+ 0.9 Q3	+ 1.6	+ 2.0	nil Sep	+ 3.4 Aug	5.4 Oct	5.0
France	+ 0.9	+ 0.8 Q3	+ 1.0	+ 1.8	– 1.1 Sep	– 1.5 Sep	9.0 Oct	8.7
Germany	+ 1.1	+ 0.4 Q3	+ 0.3	+ 1.1	– 0.7 Sep	– 1.3 Sep	10.0 Nov§	9.5
Italy	+ 1.1	+ 0.5 Q3	+ 0.4	+ 1.5	+ 1.2 Sep	– 2.7 Sep	9.0 Jul	9.5
Japan	+ 3.0	+ 1.5 Q3	– 0.5	+ 0.7	+ 5.3 Oct	– 1.9 Sep	5.5 Oct	5.4
Netherlands	+ 0.3	+ 0.1 Q3	+ 0.3	+ 1.4	– 2.3 Sep	+ 0.9 Sep	2.4 Oct**	2.0
Spain	+ 3.2	+ 1.8 Q3	+ 1.9	+ 2.4	+ 3.1 Sep	na	11.2 Sep	10.6
Sweden	+ 2.4	+ 2.1 Q2	+ 1.7	+ 2.3	+ 1.1 Sep	+ 7.4 Sep	3.7 Oct†	4.0
Switzerland	+ 1.3	+ 0.6 Q3	nil	+ 1.2	– 2.0 Q2	– 1.1 Sep	3.0 Oct†	1.9
United States	+ 4.0	+ 3.2 Q3	+ 2.4	+ 2.6	+ 1.2 Oct	+ 0.6 Oct	5.7 Oct†	5.4
Euro area	+ 1.3	+ 0.8 Q3	+ 0.7	+ 1.5	– 0.6 Sep	– 0.6 Sep	8.4 Oct	8.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	+ 8.8	+ 2.5 Q2	na	na	+ 4.3 Oct	+ 3.4 Aug	8.5 Oct†	8.3
Greece	na	+ 4.0 Q2	na	na	– 1.4 Sep	na	na	na
Iceland	na	+ 3.12001	na	na	+ 3.3 2001	na	2.2 Sep†	1.0
Ireland	na	+ 6.5 Q2	na	na	+ 8.2 Sep	+ 5.2 Sep	4.3 Oct	3.9
Luxembourg	na	+ 3.52001	na	na	– 1.9 Aug	– 5.7 Jul	3.0 Sep†	2.5
New Zealand	+ 7.1	+ 4.0 Q2	na	na	+ 4.3 Q2	+ 8.1 Q3	5.4 Q3	5.2
Norway	+ 3.1	+ 1.7 Q2	na	na	–10.1 Sep	+ 2.8 Oct	3.8 Q3	3.6
Portugal	+ 2.8	+ 0.9 Q2	na	na	– 0.5 Oct	+ 1.4 Oct	5.1 Q3†	4.0

*% change at an annual rate. †Not seasonally adjusted. ††July-Sep; claimant count rate 3.1% in Oct. §EU harmonised rate 8.4% in Nov. **Aug-Oct.

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Prices and wages

Dec 5th 2002
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2002	2003	latest		year ago	latest		year ago
Australia	+ 3.2	Q3	+ 2.5	+ 2.9	+ 2.6	– 0.2	Q3	+ 2.4	+ 3.6	Q3	+ 4.0
Austria	+ 1.8	Oct	+ 2.5	+ 1.8	+ 1.7	+ 0.3	Oct	– 0.5	+ 2.3	Oct	+ 2.8
Belgium	+ 1.3	Oct	+ 2.4	+ 1.7	+ 1.4	+ 1.5	Oct	– 4.2	+ 2.1	Q3	+ 3.7
Britain	+ 2.1	Oct	+ 1.6	+ 1.9	+ 2.4	+ 0.6	Oct	– 0.6	+ 3.8	Sep	+ 4.3
Canada	+ 3.2	Oct	+ 1.9	+ 2.2	+ 2.5	+ 2.4	Oct	– 1.3	+ 2.6	Sep	+ 2.0
Denmark	+ 2.5	Oct	+ 2.2	+ 2.4	+ 2.1	+ 0.8	Oct	– 0.3	+ 3.9	Q3	+ 4.3
France	+ 1.9	Oct	+ 1.8	+ 1.9	+ 1.4	+ 0.6	Oct	– 1.5	+ 3.4	Q3	+ 4.2
Germany	+ 1.1	Nov	+ 1.7	+ 1.4	+ 1.1	+ 0.9	Oct	– 1.1	+ 2.4	Sep	+ 2.3
Italy	+ 2.5	Nov	+ 2.8	+ 2.5	+ 2.0	+ 1.1	Oct	– 0.6	+ 2.3	Oct	+ 2.5
Japan	– 0.9	Oct	– 0.8	– 1.0	– 0.6	+ 0.3	Oct	– 0.6	+ 1.5	Oct	– 0.4
Netherlands	+ 3.4	Oct	+ 4.3	+ 3.7	+ 2.5	+ 2.2	Oct	– 1.4	+ 3.4	Oct	+ 4.9
Spain	+ 4.0	Oct	+ 3.0	+ 3.4	+ 2.7	+ 1.6	Oct	– 0.4	+ 4.0	Q2	+ 2.9
Sweden	+ 2.5	Oct	+ 2.7	+ 2.3	+ 2.0	– 1.0	Oct	+ 0.5	+ 2.7	Sep	+ 3.6
Switzerland	+ 0.9	Nov	+ 0.3	+ 0.7	+ 0.8	– 0.6	Oct	– 1.4	+ 2.5	2001	+ 1.3
United States	+ 2.0	Oct	+ 2.1	+ 1.6	+ 2.1	+ 0.6	Oct	– 0.3	+ 3.0	Oct	+ 3.8
Euro area	+ 2.2	Nov	+ 2.1	+ 2.2	+ 1.7	+ 0.9	Oct	– 0.7	+ 3.3	Q2	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.5	Oct	+ 2.2	na	na	+ 0.8	Oct	– 3.4	+ 3.5	Q3	+ 4.7
Greece	+ 3.7	Oct	+ 2.8	na	na	+ 1.9	Sep	+ 1.3	na		na
Iceland	+ 2.4	Nov	+ 8.1	na	na	+ 5.8	Nov	+ 6.8	+ 5.9	Oct	+ 9.1
Ireland	+ 4.7	Oct	+ 4.3	na	na	– 0.4	Oct	– 1.4	+ 4.3	Q2	+ 8.5
Luxembourg	+ 2.2	Oct	+ 2.3	na	na	– 0.1	Sep	– 0.6	– 1.8	Aug	+ 3.4
New Zealand	+ 2.6	Q3	+ 2.4	na	na	– 1.7	Q3	+ 6.2	+ 2.3	Q3	+ 2.0
Norway	+ 1.8	Oct	+ 2.2	na	na	+ 4.4	Oct	–19.1	+ 5.0	Q3	+ 4.8
Portugal	+ 4.0	Oct	+ 4.1	na	na	+ 1.4	Oct*	+ 1.0	+ 0.6	Sep*	na

*Revised series

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Economic forecasts

Dec 5th 2002
From The Economist print edition

The Economist poll of forecasters, December averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2002	2003	2002	2003	2002	2003	2002	2003
Australia	3.3/3.9	2.8/4.0	3.6 (3.7)	3.3 (3.5)	2.9 (2.8)	2.6 (2.5)	−3.8(−3.7)	−3.9 (−3.7)
Austria	0.3/1.0	1.0/2.5	0.6 (0.7)	1.6 (1.7)	1.8	1.7	−0.8(−1.8)	−0.9 (−1.8)
Belgium	0.3/0.8	1.3/2.4	0.6	1.7 (1.8)	1.7	1.4	5.1 (4.9)	5.0
Britain	1.4/1.8	1.7/3.5	1.6	2.5 (2.6)	1.9	2.4	−2.0(−1.9)	−2.0 (−1.9)
Canada	3.2/3.6	2.6/4.1	3.4	3.2	2.2	2.5	1.9 (2.0)	1.9 (2.1)
Denmark	1.3/2.0	1.4/2.4	1.6 (1.8)	2.0 (2.1)	2.4 (2.3)	2.1	2.2	2.0
France	0.9/1.1	1.3/2.1	1.0 (1.1)	1.8	1.9	1.4	1.6 (1.8)	1.6 (1.8)
Germany	0.2/0.4	0.6/1.5	0.3 (0.4)	1.1 (1.3)	1.4	1.1 (1.2)	1.4	1.1 (1.0)
Italy	0.3/0.5	1.1/1.9	0.4	1.5 (1.6)	2.5 (2.4)	2.0 (1.9)	nil	−0.1 nil
Japan	−1.1/nil	−0.1/2.0	−0.5 (−0.7)	0.7 (1.0)	−1.0 (−0.9)	−0.6	2.8	2.8
Netherlands	0.1/0.6	0.4/2.5	0.3 (0.4)	1.4	3.7	2.5	3.0 (3.3)	3.2 (3.6)
Spain	1.6/2.1	2.0/2.9	1.9	2.4	3.4	2.7 (2.6)	−2.1(−1.9)	−1.9 (−1.7)
Sweden	1.5/2.0	1.9/2.7	1.7	2.3 (2.4)	2.3	2.0 (2.1)	3.3	3.3
Switzerland	−0.3/1.2	0.7/2.3	nil (0.1)	1.2 (1.3)	0.7	0.8 (0.9)	10.2(10.0)	10.5 (10.3)
United States	2.3/2.6	2.0/3.3	2.4	2.6 (2.7)	1.6	2.1 (2.2)	−4.8(−4.7)	−5.0 (−4.9)
Euro area	0.5/0.9	1.2/1.8	0.7	1.5 (1.7)	2.2	1.7	0.6 (0.5)	0.6

Sources: ABN Amro, Deutsche Bank, Economist Intelligence Unit, Goldman Sachs, HSBC Securities, KBC Bank, Merrill Lynch, J.P. Morgan Chase, Morgan Stanley, Nordea, Decision Economics, BNP Paribas, Royal Bank of Canada, Schroder Salomon Smith Barney, Scotiabank, Shinsei Bank, UBS Warburg

Every month *The Economist* surveys a group of forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table also shows the highest and lowest projections for growth. The previous month's forecasts, where different, are shown in brackets. The panel has once again become gloomier about the outlook. It now expects the euro area to grow by only 1.5% in 2003, down from 1.7% in November. Germany is forecast to grow by only 0.3% in 2002 and by 1.1% in 2003. America's growth forecast for 2003 has been trimmed again. And the panel expects Japan to grow by 0.7% in 2003, down from 1.0% expected in November. Australia is doing well not just on the cricket pitch but in the growth league: it heads the table of all 15 countries both this year and next.

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Money and interest rates

Dec 5th 2002
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Dec 4th 2002)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	– 6.7	+10.1	Oct	4.84	4.25	4.77	5.52	5.54	6.64
Britain	+ 8.2	+ 5.4	Oct	3.94	3.75	4.11	4.67	4.75	5.99
Canada	+11.1	+ 6.1	Oct	2.71	2.05	3.31	5.19	5.37	6.96
Denmark	+ 4.1	+ 6.4	Oct	3.35	3.63	3.47	4.64	4.82	6.74
Japan	+29.0	+ 3.3	Oct	0.02	0.02	0.05	0.96	1.36	1.09
Sweden	+ 2.6	+ 6.7	Aug	3.80	3.75	4.04	5.01	5.11	4.73
Switzerland	+11.5	+ 5.4	Oct	0.74	1.93	1.22	2.45	3.21	3.69
United States	+ 3.5	+ 6.0	Oct	1.33	1.84	2.00	4.24	4.90	6.39
Euro area†	+ 8.2	+ 7.0	Oct	2.99	3.35	3.07	4.48	4.62	5.19

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 5.02%, Japan No.244 1.03%. Central bank rates: US fed funds 1.25%, ECB refinancing 3.25%, BOJ overnight call 0.001%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS Warburg, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Dec 5th 2002
From The Economist print edition

1995=100

	Nov 26th*	Dec 3rd*	% change on one month	% change on one year
Dollar index				
All items	76.1	76.2	+ 0.1	+15.8
Food	79.5	79.3	– 1.3	+16.3
Industrials				
All	71.4	72.1	+ 2.2	+15.0
Nfa†	73.3	73.9	+ 2.1	+27.5
Metals	69.8	70.5	+ 2.2	+ 5.8
Sterling index				
All items	76.9	76.7	– 0.2	+ 5.1
Euro index				
All items	100.8	100.5	+ 0.4	+ 3.5
Yen index				
All items	98.6	100.9	+ 2.2	+16.0
Gold				
$ per oz	318.40	319.45	+ 0.3	+15.7
West Texas Intermediate				
$ per barrel	26.41	27.32	+ 4.7	+40.8

* Provisional. † Non-food agriculturals.

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Stockmarkets

Dec 5th 2002
From The Economist print edition

Market indices

	Dec 4th	2002 high	2002 low	% change on one week	% change on record high	% change on Dec 31st 2001 in local currency	% change on Dec 31st 2001 in $ terms
Australia (All Ordinaries)	2,993.4	3,440.0	2,855.5	+ 0.8	-13.0	-10.9	- 2.5
Austria (ATX)	1,123.0	1,357.2	1,003.7	+ 1.7	-35.4	- 1.5	+10.6
Belgium (Bel 20)	2,004.7	2,899.8	1,773.7	- 4.4	-45.6	-27.9	-19.1
Britain (FTSE 100)	4,048.6	5,323.8	3,671.1	- 2.3	-41.6	-22.4	-16.2
Canada (Toronto Composite)	6,610.4	7,958.1	5,695.3	+ 0.1	-42.0	-14.0	-11.9
Denmark (KBX)	166.6	233.4	156.4	- 1.8	-44.8	-25.9	-16.7
France (SBF 250)	2,155.1	3,081.9	1,794.5	- 2.8	-50.9	-27.7	-18.8
(CAC 40)	3,199.8	4,688.0	2,656.5	- 3.4	-53.8	-30.8	-22.3
Germany (Xetra DAX)	3,320.8	5,462.6	2,597.9	- 0.8	-58.8	-35.6	-27.7
Italy (BCI)	1,162.7	1,513.0	974.4	- 0.6	-46.7	-18.9	- 8.9
Japan (Nikkei 225)	9,006.7	11,979.9	8,303.4	+ 1.5	-76.9	-14.6	-10.2
(Topix)	874.7	1,139.4	817.1	+ 0.6	-69.7	-15.3	-11.0
Netherlands (AEX)	343.3	531.2	291.4	- 4.0	-51.1	-32.3	-23.9
Spain (Madrid SE)	678.0	848.1	568.5	- 2.2	-40.8	-17.8	- 7.6
Sweden (Affarsvarlden Gen)	161.2	236.8	122.7	- 2.8	-59.7	-30.3	-19.4
Switzerland (Swiss Market)	5,010.4	6,694.1	4,435.0	- 3.3	-40.4	-21.9	-12.0
United States (DJIA)	8,737.9	10,635.3	7,286.8	- 2.2	-25.5	-12.8	-12.8
(S&P 500)	917.6	1,172.5	776.8	- 2.3	-39.9	-20.1	-20.1
(NASDAQ Comp)	1,430.4	2,059.4	1,114.1	- 3.9	-71.7	-26.7	-26.7
Europe (FTSE Eurotop 300)*	913.9	1,279.7	797.2	- 2.4	-46.4	-27.5	-18.6
Euro area (FTSE Ebloc 100)*	774.3	1,125.1	639.4	- 2.7	-50.1	-30.4	-21.8
World (MSCI)†	815.7	1,024.4	703.7	- 1.8	-43.7	na	-18.7
World bond market (Salomon)‡	499.5	510.0	430.3	+ 0.1	- 2.1	na	+13.6

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡Salomon Smith Barney World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Dec 5th 2002
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2002	2003	Exchange rate trade-weighted† 1990=100 Dec 4th	year ago	Currency units per $ Dec 4th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2002‡
Australia	− 3.3	Oct	− 14.3	Q3	− 3.8	− 3.9	75.0	72.8	1.78	1.94	2.81	1.78	1.43	0.1
Austria	− 0.8	Aug	− 1.1	Sep	− 0.8	− 0.9	100.8§	100.3	1.00	1.13	1.57	–	0.80	-1.6
Belgium	+ 17.1	Sep	+ 12.4	Jun	+ 5.1	+ 5.0	100.0§	99.7	1.00	1.13	1.57	–	0.80	nil
Britain	− 46.1	Sep	− 25.8	Q2	− 2.0	− 2.0	106.2	104.9	0.64	0.71	–	0.64	0.51	-1.4
Canada	+ 34.7	Sep	+ 12.4	Q3	+ 1.9	+ 1.9	76.3	76.7	1.56	1.57	2.45	1.56	1.25	0.6
Denmark	+ 7.1	Sep	+ 3.6	Sep	+ 2.2	+ 2.0	103.3	102.3	7.43	8.38	11.7	7.43	5.95	2.2
France	+ 9.8	Sep	+ 26.8	Sep	+ 1.6	+ 1.6	102.9§	101.9	1.00	1.13	1.57	–	0.80	-2.7
Germany	+110.9	Sep	+ 37.6	Sep	+ 1.4	+ 1.1	99.9§	98.7	1.00	1.13	1.57	–	0.80	-3.7
Italy	+ 11.6	Sep	− 1.0	Sep	nil	− 0.1	73.4§	72.7	1.00	1.13	1.57	–	0.80	-2.3
Japan	+ 86.5	Sep	+113.1	Sep	+ 2.8	+ 2.8	128.8	136.1	125	124	196	125	–	-7.9
Netherlands	+ 27.2	Sep	+ 9.0	Q3	+ 3.0	+ 3.2	99.1§	98.1	1.00	1.13	1.57	–	0.80	-0.8
Spain	− 36.9	Sep	− 14.2	Aug	− 2.1	− 1.9	75.0§	74.3	1.00	1.13	1.57	–	0.80	nil
Sweden	+ 14.2	Oct	+ 8.0	Sep	+ 3.3	+ 3.3	78.4	74.4	9.07	10.6	14.3	9.07	7.27	1.7
Switzerland	+ 4.4	Oct	+ 22.7	Q2	+10.2	+10.5	114.4	111.9	1.47	1.66	2.31	1.47	1.18	na
United States	−452.7	Sep	−428.8	Q2	− 4.8	− 5.0	113.9	120.2	–	–	1.57	1.00	0.80	-3.1
Euro area	+ 95.6	Sep	+ 38.0	Sep	+ 0.6	+ 0.6	82.8	78.7	1.00	1.13	1.57	–	0.80	-2.2
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.1	Sep	+ 9.5	Sep	na	na	79.0§	78.9	1.00	1.13	1.57	–	0.80	3.2
Greece	− 20.3	Sep	− 7.7	Aug	na	na	58.0§	57.6	1.00	1.13	1.57	–	0.80	-1.1
Iceland	+ 0.2	Oct	− 0.1	Q2	na	na	93.0**	87.8	85.1	108.7	134	85.1	68.2	0.3
Ireland	+ 34.7	Sep	+ 0.4	Q2	na	na	89.1§	87.7	1.00	1.13	1.57	–	0.80	-0.5
Luxembourg	− 2.6	Aug	+ 2.1	Q2	na	na	100.0§	99.2	1.00	1.13	1.57	–	0.80	1.8
New Zealand	− 0.4	Oct	− 1.3	Q2	na	na	91.6	79.1	2.00	2.41	3.14	2.00	1.60	1.6
Norway	+ 24.5	Oct	+ 25.6	Sep	na	na	107.1	96.2	7.27	8.99	11.4	7.27	5.83	12.4
Portugal	− 12.7	Aug	− 9.8	Sep	na	na	91.2**	89.5	1.00	1.13	1.57	–	0.80	-3.4

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, September average. ‡OECD forecast. **IMF, July average.

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International investment position

Dec 5th 2002
From The Economist print edition

The Swiss had a net $300 billion invested abroad in 2000, over 100% of Swiss GDP. But America was a net recipient of global savings, reflecting its huge current-account deficit.

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Overview

Dec 5th 2002
From The Economist print edition

South-East Asia's economies are taking steps towards recovery. **Hong Kong's** economy grew by 3.3% in the year to the third quarter; industrial production in **Thailand** grew by 8.9% in the year to October.

Latin America is making rather less confident strides out of its downturn. **Colombia's** war-torn economy chalked up only a 1.9% growth rate in the year to the third quarter, and its industrial output grew by 2.8% in the year to September. **Brazil's** GDP grew by 2.4% in the year to the third quarter. But inflation is surging in **Venezuela,** where consumer prices rose by 30.7% in the 12 months to November.

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Fertility

Dec 5th 2002
From The Economist print edition

Controlling fertility is crucial to bridge the gap between rich and poor, according to *State of World Population 2002*, a report from the United Nations Population Fund. Poor young women in Latin America and East Asia have more than five times as many children as the rich. Unwanted pregnancies can undermine mothers as well as babies; women in poor countries, such as Liberia, are 600 times more likely to die in pregnancy and birth than women in rich countries. The report argues that greater access to contraception and more female education would help to lower birth rates.

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Economy

Dec 5th 2002
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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 8.1	Q3	+14.2	Oct	– 0.8	Oct	+30.0	Oct	+17.4	2001	258.6	Sep
Hong Kong	+ 3.3	Q3	–11.2	Q2	– 3.6	Oct	– 7.7	Oct	+15.7	Q2	110.6	Oct
India	+ 6.0	Q2	+ 6.1	Sep	+ 4.1	Oct	– 6.1	Oct	+ 2.0	Q2	60.7	Oct
Indonesia	+ 3.9	Q3	–11.7	Q1	+10.5	Nov	+26.3	Oct	+ 6.9	Q2	29.0	Oct
Malaysia	+ 5.6	Q3	+ 9.0	Sep	+ 2.1	Oct	+13.0	Oct	+ 6.9	Q2	32.7	Oct
Philippines	+ 3.8	Q3	– 4.9	Sep	+ 2.5	Nov	+ 2.6	Sep	+ 5.9	Aug	13.1	Oct
Singapore	+ 3.7	Q3	+11.8	Oct	– 0.2	Oct	+ 7.8	Oct	+18.9	Q3	81.4	Oct
South Korea	+ 5.8	Q3	+12.7	Oct	+ 3.5	Nov	+11.3	Nov	+ 6.2	Oct	116.3	Oct
Taiwan	+ 4.8	Q3	+ 7.4	Oct	– 1.7	Oct	+17.8	Oct	+25.0	Q3	157.6	Oct
Thailand	+ 5.1	Q2	+ 8.9	Oct	+ 1.4	Oct	+ 4.7	Oct	+ 6.9	Sep	36.4	Oct
Argentina	–13.6	Q2	– 3.4	Oct	+40.5	Nov	+14.9	Sep	+ 3.9	Q2	9.4	Sep
Brazil	+ 2.4	Q3	+ 5.6	Sep	+ 8.5	Oct	+11.2	Oct	–10.8	Oct	38.4	Sep
Chile	+ 1.8	Q3	+ 5.2	Sep	+ 3.0	Oct	+ 2.6	Oct	– 0.6	Q2	14.9	Oct
Colombia	+ 1.9	Q3	+ 2.8	Sep	+ 6.4	Oct	+ 0.5	Aug	– 1.3	Q2	10.6	Oct
Mexico	+ 1.8	Q3	– 0.6	Sep	+ 4.9	Oct	– 8.8	Oct	–16.1	Q3	46.1	Oct
Peru	+ 7.3	Sep	+ 7.6	Sep	+ 1.5	Nov	+ 0.3	Sep	– 1.0	Q3	9.4	Oct
Venezuela	– 5.5	Q3	– 6.6	Jul	+30.7	Nov	+ 8.5	Q2	+ 4.9	Q3	8.2	Sep
Egypt	+ 4.9	2001†	+ 7.8	2001†	+ 2.8	Oct	– 7.9	Jul	nil	Q2	12.8	Aug
Israel	– 0.8	Q3	– 0.2	Sep	+ 6.9	Oct	– 6.4	Oct	– 2.6	Q2	24.4	Oct
South Africa	+ 3.1	Q3	+ 8.6	Sep	+14.5	Oct	+ 3.7	Oct	– 0.3	Q2	6.0	Oct
Turkey	+ 8.2	Q2	+11.8	Oct	+31.8	Nov	–11.7	Sep	+ 0.8	Sep	25.6	Oct
Czech Republic	+ 2.5	Q2	+ 9.2	Sep	+ 0.6	Oct	– 3.0	Oct	– 4.2	Q3	22.5	Oct
Hungary	+ 3.4	Q3	+ 8.1	Sep	+ 4.9	Oct	– 2.9	Oct	– 2.9	Oct	9.7	Oct
Poland	+ 0.8	Q2	+ 3.2	Oct	+ 1.1	Oct	–10.1	Oct	– 6.3	Oct	28.2	Oct
Russia	+ 4.1	Q2	+ 3.9	Oct	+14.9	Oct	+42.9	Sep	+27.6	Q3	43.0	Oct
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.3	2001†	– 0.5	Jun	+ 3.5	Oct	– 1.2	Oct	+ 2.7	2002†	6.8	Oct
Saudi Arabia	+ 1.2	2001	na		– 1.1	Jul	+44.1	2001	+14.5	2001	20.2	Oct

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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Financial markets

Dec 5th 2002
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Dec 4th		Dec 31st 2001	
	Dec 4th	year ago	Dec 4th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	13.0	na	1,478.7	+2.6	– 13.7	– 13.7
Hong Kong	7.80	7.80	12.3	1.56	9,995.7	+0.5	– 12.3	– 12.3
India	48.2	47.9	75.7	5.10	3,207.4	+1.0	– 1.7	– 1.6
Indonesia	8,990	10,470	14,130	13.78	397.1	+3.7	+ 1.3	+ 17.2
Malaysia	3.80	3.80	5.97	3.10	618.4	–2.2	– 11.2	– 11.2
Philippines	53.6	52.0	84.2	6.81	1,036.3	nil	– 11.3	– 14.6
Singapore	1.77	1.83	2.78	0.81	1,366.0	–2.1	– 15.9	– 12.3
South Korea	1,216	1,266	1,912	4.90	714.5	+0.9	+ 3.0	+ 11.2
Taiwan	34.8	34.4	54.7	1.80	4,727.5	+2.0	– 14.8	– 14.3
Thailand	43.7	44.0	68.7	1.93	364.9	+1.0	+ 20.1	+ 21.5
Argentina	3.54	1.01	5.56	7.00	515.1	+1.1	+ 74.4	– 50.7
Brazil	3.70	2.43	5.82	21.90	10,640.1	+4.0	– 21.6	– 51.1
Chile	711	673	1,118	2.76	4,813.6	+0.5	– 10.8	– 17.1
Colombia	2,808	2,315	4,413	7.91	1,487.5	+3.3	+ 38.9	+ 12.7
Mexico	10.23	9.22	16.1	6.37	6,187.7	+1.0	– 2.9	– 13.0
Peru	3.55	3.43	5.59	3.97	1,380.3	+1.9	+ 17.4	+ 13.8
Venezuela	1,317	748	2,070	30.45	8,015.2§	+1.8	+ 22.0	– 29.8
Egypt	4.63	4.27	7.28	6.17	5,424.7	+4.0	+ 2.9	+ 1.6
Israel	4.65	4.23	7.31	6.40	361.0	+0.9	– 19.2	– 23.4
South Africa	9.2	10.80	14.4	13.60	9,529.0	+1.7	– 8.7	+ 19.5
Turkey	1,549,000	1,456,000	2,434,563	41.00	13,287.3	+1.9	– 3.6	– 9.4
Czech Republic	31.0	37.2	48.8	2.74	449.8	–3.4	+ 14.0	+ 30.6
Hungary	237	281	373	8.69	8,020.1	nil	+ 12.5	+ 30.3
Poland	3.98	4.08	6.26	6.68	14,838.1	–0.1	+ 6.6	+ 5.8
Russia	31.9	30.0	50.1	21.00	346.1‡	–2.8	+ 39.0	+ 33.1
EMF (MSCI)*	1.00	1.00	1.57	na	300.3	+0.6	na	– 5.4
EMBI+†	1.00	1.00	1.57	na	222.9	+0.9	na	+ 11.3

*Emerging Mkts Free. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡ In $ terms. §Nov 29th.

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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